No. 75-1872

In the Supreme Court of the United States

OCTOBER TERM, 1975

SECURITIES AND EXCHANGE COMMISSION, PETITIONER

v.

RICHARD J. COLLINS, ET AL.

APPENDIX TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

ROBERT H. BORK,
Solicitor General,
Department of Justice,
Washington, D.C. 20530.

DAVID FERBER,
Solicitor to the Commission,

JACOB H. STILLMAN,
Assistant General Counsel,

JAMES E. MILLER,
Attorney,
Securities and Exchange Commission,
Washington, D.C. 20549.

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APPENDIX A

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.

INVESTMENT COMPANY ACT OF 1940
Rel. No. 8615/December 13, 1974

Admin. Proc. File No. 3-3928

In the Matter of

CHRISTIANA SECURITIES COMPANY
Wilmington, Delaware

E. I. DU PONT DE NEMOURS AND COMPANY
Wilmington, Delaware
(812-3224)

FINDINGS AND OPINION OF THE COMMISSION

MERGER OF A REGISTERED INVESTMENT COMPANY INTO ITS AFFILIATE

I

This case involves one of the world's great industrial complexes. It is here under the Investment Company Act of 1940. Its origins, however, go back to 1915.

At that time T. Coleman du Pont[1] was the largest single stockholder of E. I. du Pont de Nemours and Company ("Du Pont").[2] He wished to dispose of that

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[1] The duPont family spells its name with a lower-case "d."

[2] In this opinion the company's name is hereinafter spelled with an upper-case "D."

interest. To keep Coleman's large block of stock within the family thus assuring its continued control of the enterprise, Coleman's cousin Pierre joined with others to form a holding company.[3] That was Christiana Securities Company.[4] It began life with the substantial amount of Du Pont stock acquired from Coleman plus other blocks of that security contributed by Pierre and by other family members in exchange for Christiana shares.[5] Thus Christiana was organized by members of the du Pont family for the service of their own interests. Through Christiana, the family's dominant faction made sure that its massive holdings in Du Pont would be voted as a block.[6] Christiana was a control device. Historians friendly to Pierre and to the family point out that:

> "[I]t was as chairman of the Christiana Securities Company that his power was most explicitly defined. His immediate family held over 60% of Christiana common stock, and Christiana in turn held over 30%

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[3] With one exception, all of the people involved were members of the du Pont family. And the outsider was a man closely linked to the family.

[4] Christiana was at first called Du Pont Securities Company. It took its present name in 1918.

[5] The historical treatment is based on CHANDLER & SALSBURY, PIERRE S. DU PONT AND THE MAKING OF THE MODERN CORPORATION 322-358 (1971). For other accounts see JAMES, ALFRED I. DU PONT: THE FAMILY REBEL (1941) (critical of Pierre and his associates and castigating them as "the secret six"); DONALDSON, CAVEAT VENDITOR (privately printed 1964) presenting the situation from Coleman's viewpoint.

[6] The historical writings cited in the preceding footnote show that a family feud between Pierre and his cousin Alfred had much to do with Christiana's origins.

of the Du Pont common stock outstanding (through Delaware Realty[7] and personal holdings the share held by Pierre's family in Du Point was even higher). Since the Du Pont Company still owned close to 35% of the voting stock of General Motors, the family had practical control of that corporation."[8]

II

The du Point family is large. And since the family rewarded outstanding managerial performance with Christiana stock, there were some non-du Pont stockholders in Christiana from the very beginning.[9] So by 1940, when the Investment Company Act went into effect, Christiana had far more than a handful of stockholders.

Christiana registered under the Act. It had to do so for two reasons:

(A) Christiana had more than the 100 security holders whose presence, with other facts, brings the Act into play.[10]

(B) Christiana maintained, and still maintains, that it did not and does not run Du Pont. It insists that it is not Du Pont's parent. It concedes that it "has the

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[7] See *Delaware Realty and Investment Company*, 40 S.E.C. 469 (1961) (Footnote added).

[8] CHANDLER & SALSBURY, PIERRE S. DU PONT AND THE MAKING OF THE MODERN CORPORATION 564-565 (1971). On page 565 the authors note that "During the 1920s Pierre and his brothers were obsessively concerned about assuring control."

[9] CHANDLER & SALSBURY, PIERRE S. DU PONT AND THE MAKING OF THE MODERN CORPORATION 581 (1971).

[10] Section 3(c)(1).

potential to exercise a controlling influence over Du Pont," but it has consistently contended that this potential lies dormant and unexercised and that there is no actual control relationship. This, its own version of the facts, made, and makes, Christiana an investment company of the closed-end, non-diversified type rather than an industrial holding company.[11]

III

Today Christiana is still what it was at its birth in 1915, a receptacle for a huge block of Du Pont common stock. It holds 28.3% of the issue. This massive commitment accounts for something like 98% of Christiana's total assets.[12]

Christiana's stock is still highly concentrated. While it has over 11 million common shares outstanding, 95.5% of them are held by a mere 338 people. Christiana remains in overwhelming measure a du Pont family affair, 75% of its outstanding shares being held by family members.

This does not mean that Christiana is just a collective name for the descendents of the original stockholders. It is a publicly held company with about 8,000 stockholders. There is an over-the-counter market in the issue, and for reasons hereinafter explained, Christiana

[11] For fuller discussion see this Commission's 1966 report on the PUBLIC POLICY IMPLICATIONS OF INVESTMENT COMPANY GROWTH, House Report No. 2337, 89th Cong., 2d Sess. 40, n. 54.

[12] It also holds a small block of Du Pont preferred. The non-Du Pont assets consist of the two daily newspapers in Wilmington, Delaware, and 3.5% of the stock of the Wilmington Trust Company. *Qua* trustee for various du Ponts and du Pont relatives, the Trust Company holds more than half of Christiana's common stock.

shares have over the years had a certain appeal to a few of the many people who wanted to invest in Du Pont. It was—and for that matter, still is—cheaper to buy into Du Pont indirectly by buying Christiana than it was to acquire the underlying Du Pont shares themselves. Someone with $10,000 that he wanted to invest in Du Pont common could do so in one of two ways. The first was to buy $10,000 worth of Du Pont on the New York Stock Exchange. The second was to buy $10,000 worth of Christiana in the over-the-counter market. Since Christiana, like most other closed-end investment company issues, has long tended to sell at a substantial discount from net asset or liquidation value, the Christiana buyer got what could be regarded as a real bargain. His $10,000 purchased an interest in Du Pont that might have cost him $12,000, $13,000 or $14,000 had he acquired it in the direct Du Pont form rather than in the indirect Christiana form. One did not have to be a du Pont in order to see the point. The record suggests that some of the 338 large holders previously referred to may be wholly unconnected with the founding family. Although members of the du Pont family still hold about 75% of Christiana, the other 25% belongs to public investors.

IV

Those who control Christiana (and who presumptively at least are for present purposes deemed to control Du Pont as well [13]) think that Christiana has outlived its usefulness. Du Pont, they say, is no longer a

[13] Under Section 2(a)(9) of the Act an interest of more than 25% in voting securities is presumed to constitute control. We also note that Christiana and Du Pont have five common directors.

family firm. Hence the family no longer needs Christiana. It has no contemporary function.

And Christiana is expensive. It costs something to run. Much more important than administrative costs are the taxes that have to be paid because of Christiana's existence. For practical purposes, Christiana's income consists entirely of the dividends it collects from Du Pont. Yet Federal income tax has to be paid on those dividends before they can be distributed to Christiana's stockholders. Were there no Christiana and were the present Christiana stockholders to own their Du Pont shares directly, there would be no such tax.

Accordingly, Christiana's management urges that Christiana merge into its portfolio company, Du Pont. Du Pont's management agrees.[14] The salient features of the joint Christiana-Du Pont proposal are these:[15]

(1) Christiana's assets and liabilities will become those of Du Pont.[16]

(2) Accordingly, Du Pont will reacquire the 13,417,120 shares of its own common now in Christiana's portfolio.[17] Those shares will be retired.

(3) Each Christiana common share will become 1.123 shares of Du Pont.[18]

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[14] In addition to the five common directors referred to in the preceding footnote, another seven of Du Pont's 26 directors own Christiana common stock.

[15] The application before us states that the 12 Du Pont directors who are also directors or stockholders of Christiana did not participate in the consideration of the merger proposal.

[16] Du Pont intends to dispose of the newspaper interests and the bank stock (see n. 12 on p. 5, *supra*) to be acquired from Christiana.

[17] Christiana's 16,256 shares of Du Pont's $4.50 preferred (0.96% of the outstanding shares of that class) will also be reacquired by Du Pont.

[18] In time the present Christiana holders may also receive some

The merger is designed to be tax-free to Christiana and its stockholders. Accordingly, it is conditioned on a ruling to that effect by the Internal Revenue Service.

V

Like other corporate mergers, this one cannot be consummated unless the law of the state of incorporation (in this case Delaware for both companies) is followed. Hence the stockholders of both companies must approve. Were this an ordinary amalgamation between industrial or mercantile firms, the merits of the matter would be none of our concern. Our responsibility would be solely that of seeing to it that the two companies' stockholders were told enough about the proposal to enable them to reach an informed judgment. The decision would be theirs, not ours.

But Christiana is an investment company, and the

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additional Du Pont stock. This would stem from a contingent, unliquidated tax refund claim that Christiana now has against the United States. Du Pont will acquire that claim. If it collects on it within five years from the effective date of the merger, it will distribute additional shares of its common whose then current market value will equal the proceeds of the claim. Should the tax refund claim remain unsettled and unadjudicated within the aforementioned five-year period, the number of additional shares issued will be based on the then fair value of the claim.

The plan makes provision for the holders of Christiana's 106,500 7% callable preferred. Those shares are callable at $120. Accordingly, the plan calls for their conversion into shares of Du Pont with a then market value of $120, based on the average closing price of Du Pont common stock on the New York Stock Exchange for the ten trading days immediately preceding the effective date of the merger, plus cash equal to the accrued dividend. Du Pont states that its present intention is to offer dissenting Christiana preferred holders who follow Delaware's statutory appraisal procedures $120 in cash (plus the accrued dividend) for each share.

Congress that passed the Investment Company Act deemed transactions of this character to be fraught with potential for overreaching and unfairness.[19] Accordingly, it prohibited them,[20] subject to our power to lift the prohibition [21] "if evidence establishes that . . . the terms of the proposed transaction, including the consideration to be paid or received, are reasonable and fair and do not involve overreaching on the part of *any* person [22] concerned." [23]

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[19] Section 1(b)(2) of the Act states that "the national public interest and the interest of investors are adversely affected—when investment companies are . . . managed . . . in the interest of directors, officers, . . . or other affiliated persons thereof . . ., in the interest of special classes of their security holders, or in the interest of other investment companies or persons engaged in other lines of business, rather than in the interest of all classes of such companies' security holders." Of special significance here is Section 1(b)(2)'s reference to investment companies' affiliated persons. Christiana and Du Pont are "affiliated persons" of each other. That is so because Christiana owns more (far more) than 5% of Du Pont's voting securities. See Sections 2(a)(3)(A) and 2(a)(3)(B).

[20] Section 17(a)(1) of the Act makes it "unlawful for any affiliated person [of] . . . a registered investment company . . . knowingly to sell any security or other property to such registered company." The proposed combination would take the form of a statutory merger. But this would constitute a "sale" by Christiana of its assets to Du Pont within the meaning of Section 17(a)(1). *E. I. du Pont de Nemours & Company*, 34 S.E.C. 531 (1953), overruling *Phoenix Securities Corporation*, 9 S.E.C. 241 (1941).

[21] Section 17(b) provides that "notwithstanding subsection (a), any person may file with the Commission an application for an order exempting a proposed transaction. . . . The Commission *shall* [emphasis added] grant such application and issue such order of exemption if. . . ."

[22] Because of its special impact here the word "*any*" has been italicized. Its presence means that we must find this transaction fair to the stockholders of both companies. See *Bowser, Inc.*, 43 S.E.C. 277 (1967).

As we said in *Fifth Avenue Coach Lines, Inc.*, 43 S.E.C. 635, 639

Does this transaction meet that test? That is the central question before us.[24] A negative answer will end the matter. Should our answer be in the affirmative, the managers of both companies will be at liberty to proceed to seek the approval of their stockholders.

VI

At first blush it is hard to see a real problem here. In economic reality Christiana stock already is Du Pont stock—under another name. Substantially, all that we are dealing with is an exchange of equivalents.

Christiana owns 13,417,120 shares of Du Pont com-

(1967): "[T]hat Section 17(a) by its terms makes it unlawful for the affiliate, rather than the investment company, to engage in specified types of transactions, does not . . . indicate a Congressional concern for the shareholders of the investment company to the exclusion of the other stockholders affected. While it is true that the protection of fund shareholders was a primary consideration which led to the passage of the Act, we find nothing in the legislative history which persuades us that Congress intended the broad language of Section 17(b) to be read in the restrictive manner which applicants suggest, nor have we ever done so. We cannot believe the Congress intended, after requiring an agency of the Government to examine a transaction such as this, to put that agency in the position of effectively authorizing the transaction when there are circumstances raising questions as to possible overreaching of a person concerned which has public investors."

[23] Section 17(b)(1).

[24] But it is not the only question presented. Under Section 17(b)(2) we must also find the proposed transaction consistent with Christiana's policy. And Section 17(b)(3) precludes approval unless we find the merger consistent with the Act's general purposes. Its primary general purpose, of course, is the protection of investors. Finally, the parties invoke Section 17(d) and our Rule 17d-1 thereunder, which taken together prohibit joint enterprises and joint arrangements between investment companies and persons affiliated with them, unless we approve the specific transaction involved.

mon. But there are only 11,710,103 Christiana common shares outstanding. It follows that a Christiana common share is in economic substance 1.15 shares of Du Pont common. Make a few simple adjustments for the relatively inconsequential preferred stocks of the two companies and for the newspaper interests and the bank stock that Du Pont will get from Christiana,[25] and the whole thing is over.

That in essence is the view of the two companies involved. Our Division of Investment Management Regulation agrees. But three Du Pont stockholders disagree.[26]

VII

The objecting Du Pont stockholders consider the view just outlined misleadingly simplistic. They contend that this transaction will:

(A) Confer great benefits on Christiana's stockholders;

(B) Give Du Pont's stockholders nothing worth mentioning but actually injure them; and

(C) Serve no real business purpose for Du Pont.

VIII

The objectors are clearly right when they say that the merger will be a very good thing indeed for Christiana's stockholders. Their benefits will stem from:

(A) The federal tax structure; and

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[25] See n. 12 on p. 5, *supra*.

[26] These stockholders, Lewis C. Murtaugh, Richard J. Collins, Jr. and Daniel W. Maher, participated in the hearings before the administrative law judge. An initial decision having been waived, the case came to us after the record was closed. Briefs were filed, and we heard oral argument. Our findings are based on an independent review of the record.

(B) Stock market phenomena.

I begin with the tax factors. There are two of them. One is the federal corporate income tax that Christiana now pays.[27] The United States Treasury takes 7.2 cents out of every dollar of dividend income that Christiana gets before such dividend income is disbursed to the Christiana stockholders.[28] So the merger will increase each Christiana stockholder's individual pre-tax income by 7.2% over what he would receive if Du Pont dividends continued to be passed through Christiana.[29] Of course, this 7.2% accretion will be taxable income in the individual stockholder's hands. A particular Christiana stockholder's net tax benefit will therefore depend on the tax bracket in which he happens to find himself. To the extent that Christiana stock is held by people in high tax brackets, the actual increment to

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[27] Many closed-end investment companies do not pay federal corporate income taxes. They, like most of the open-end companies, avail themselves of the special treatment that Subchapter M of the Internal Revenue Code gives to so-called regulated investment companies, i.e., companies regulated by this Commission under the Investment Company Act. Such companies are free from all corporate income taxes so long as they distribute all of their income to their stockholders. But this special tax benefit is available only to "diversified" investment companies. Christiana, of course, is as undiversified as an investment company can possibly be. Hence its federal income tax status is no different from that of any other corporation. Sections 851-855 of the Internal Revenue Code.

[28] The applicable normal corporate income tax is 48%. Section 11 of the Internal Revenue Code. But *all* corporations (whether investment companies or not) are entitled to deduct from their income 85% of any dividends that they receive. Section 243 of the Code. Thus the maximum effective federal corporate income tax on dividend income is 48% of 15% or 7.2%.

[29] Christiana pays out substantially all of its after-tax income in dividends.

the Christiana stockholders' net after taxes will be significantly less than 7.2%.[30] The second tax factor relates to the tax cost of alternative methods of achieving the end that the applicants wish to reach. Christiana could be killed off without any need for our prior (or for that matter subsequent) approval. Nothing in the Act or anywhere else in the law inhibits a registered investment company from liquidating. But a liquidation might be much more expensive for Christiana's stockholders than this tax-free plan.[31] Liquidation would certainly be a great deal more conjectural.[32]

In view of what has just been said about the special 7.2% tax burden on Christiana's stockholders, it would be unsurprising to find Christiana's shares selling at a discount of about that magnitude from net asset value.[33] Actually, however, the discount has been much

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[30] Additional savings will stem from the elimination of Christiana's operating expenses. The application states, however, that those expenses are "relatively minor."

[31] Christiana's tax picture is said to be clouded by reason of the distributions of General Motors common stock resulting from the antitrust divestiture decree entered against Du Pont. *United States v. E. I. du Pont de Memours & Co.*, 366 U.S. 316 (1961). We are told that this is so because:

"(a) the fair market value of the General Motors stock received by Christiana pursuant to the antitrust divestiture decree . . . is the subject of a tax refund suit by Christiana against the United States Government and is thus presently indeterminable;

(b) the effect of pro rata distributions by Christiana of General Motors stock to its own stockholders is uncertain under the tax laws; and

(c) the effect of distributions by Christiana of General Motors and Hercules Powder Company stock . . . is uncertain."

[32] Christiana's brief states that its "stockholders would in effect be voting tax litigation for themselves were they to sanction a liquidation."

[33] Implicit in this statement is the somewhat unrealistic assump-

higher than that. When the merger negotiations were first announced it was 23%. During the preceding two years it had been as high as 25% and was never below 20%.

The mere announcement of the planned merger led to an appreciable narrowing of the discount. Its consummation will, of course, extinguish the discount forever. Thus the merger will substantially enhance the market value of the Chistiana stockholders' property.

What is the offsetting benefit to Du Pont's stockholders? Applicants point to the fact that Christiana's stockholders will get only 97.5% of its adjusted net asset value. This looks like a 2.5% discount from net asset value. But the actual dilution to be suffered by the Christiana stockholders will be only 1.8%. That is so because Christiana is so substantial a Du Pont stockholder. Since Christiana has a 28.3% interest in Du Pont, 28.3% of the 2.5% discount will go right back into the Christiana holders' pockets. Accordingly, objectors dismiss the discount as derisory, a mere "pacifier."

The objectors' claim of positive harm to themselves and the other similarly situated Du Pont stockholders rests entirely on market factors.[34] They point out that from a stock market point of view Christiana's massive

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tion of a market for Du Pont common that is entirely income-oriented.

[34] Some Du Pont stockholders are also Christiana stockholders. Objectors do not weep for them. Their concern is with the people whose interest in Du Pont stems entirely from their ownership of its stock. Since there are over 225,000 Du Pont holders as against a mere 8,000 Christiana holders, it is obvious that most Du Pont stockholders belong to the class whose interests the objectors champion.

block of Du Pont is sterilized. Christiana has never sold any of its Du Pont. Nor, so long as it remains in being, is Christiana ever likely to do so.

The enormous capital gains taxes that would have to be paid are enough in themselves to inhibit Christiana from selling any of its Du Pont holdings. Those taxes would arise at two levels. First, at the corporate level there would be a very heavy tax on Christiana itself. The basis of its Du Pont shares is but a tiny fraction of those shares' present value. And should Christiana follow its past practice of distributing all of its income to its stockholders, a second onerous tax would fall on the individuals who own Christiana.

Most of Christiana's stock has a very low basis in the hands of those who now hold it. That is so because:

(A) The holders either paid much less for it than it is now worth or acquired it from donors who bought it for far less than present value; and

(B) The basis of their Christiana shares has already been materially reduced by reason of their receipt of substantial quantities of General Motors stock, pursuant to the Du Pont divestiture distribtuion.[35]

The objectors say that the merger will work a radical change in this state of affairs. They note that the corporate capital gains tax inhibition will vanish. After Christiana is dead and gone, no one will worry about the capital gains taxes that it would have had to pay had it remained alive. True, the holders of about 70% of Christiana's stock state that they have no present

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[35] See n. 31 on pp. 10-11, *supra*. Some 3 million Christiana shares (roughly 25% of the issue) have a zero basis.

intention of selling the Du Pont shares to be received in exchange for their Christiana holdings. But the objectors point out that:

(A) No binding commitments to refrain from selling have been given.[38]

(B) The plan's carefully crafted provisions for Securities Act registration statements at the selling stockholders' expense (twice a year on a non-firm commitment basis and once a year on the basis of a firm commitment underwriting for at least $25 million) show that some important holders have given some thought to some selling at some time.

(C) Public investors unrelated to Christiana's control group own about 25% of the company's stock. Hence the merger will give them about 3¼ million shares of Du Pont common. They will be as free as other noncontrolling Du Pont stockholders to sell those shares whenever and wherever they choose without registering them under the Securities Act.

Objectors argue that the merger will have an adverse impact on them even if nobody actually sells. They ask us to focus on potential available supply. Such supply will, they say, be increased by over 13 million shares. The market's knowledge of this is bound to depress the price. Ergo, Christiana should be required to compensate the Du Pont stockholders for the "vast and

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[38] Indeed, the Wilmington Trust Company, record owner of more than half of Christiana's outstanding shares (see n. 12 on p. 5, *supra*) states that its fiduciary responsibilities may require it to do some selling from time to time.

virtually uncontrolled increase in the supply of marketable stock'' flowing from the merger.

As for Du Pont, objectors argue that it has been doing well all these years and will continue to do well with or without Christiana; that applicants have failed to show that Christiana is an incubus to Du Pont; and that though the proposal does a great deal for the du Pont family, it does nothing of consequence for Du Pont. True, after the merger's consummation Du Pont will have about 188,500 fewer common shares outstanding than it now does. But presently outstanding shares of that issue number 47,445,810. So the number of shares outstanding will be diminished by a mere four-tenths of one percent.

One objector argues for a substantial increase in the contemplated 2.5% or 1.8% (depending on whether one looks at gross or at net impact) discount from Christiana's net asset value.[37] The other two also urge an increase in the discount. But they go on to attack the whole affair root and branch. They consider it an outrageous assault on the rights of the Du Pont stockholders and on the law of supply and demand. What they deem essential are conditions to "protect the price of Du Pont shares." They therefore implore us to impose restraints on the alienability of the new Du Pont common shares to be issued pursuant to the merger.

IX

Applicants consider the objectors' contentions frivolous and absurd. So does our Division of Investment

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[37] See p. 11, *supra*.

Management Regulation.[38] We take a different view. To us the questions presented are substantial and troublesome. This is not an easy case. But after careful consideration of the issues raised, we find ourselves constrained to resolve them against the objectors and to grant the application before us.

That there is an imbalance of benefit is plain. This

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[38] Though in accord with the applicants on every substantive point presented, the Division has certain qualms about the performance of the financial experts who testified on their behalf with respect to the value of Christiana's Du Pont holdings. It asks us to say some harsh words about those experts and to make a pronouncement about the role of an independent expert in a proceeding of this character. We agree with the Division that financial experts should be diligent, conscientious, and painstaking. On the record before us, we think it inappropriate to go beyond that truism. The importance of expert testimony varies from case to case. In some situations such testimony is crucial. When a closely held firm or a business of an esoteric character must be appraised, much turns on what the experts say. *La Salle Street Capital Corporation*, Investment Company Act Release No. 6693 (August 23, 1971) is illustrative. That case presented a question about the value of a major league baseball franchise. Such questions are, as was said at page 7 of the *La Salle Street* opinion, "not susceptible to precise determination." The instant case, on the other hand, involves marketable securities. The questions presented are in our view essentially legal. Hence they cannot be resolved by reference to the opinions of financial experts, however conscientious and however eminent. We do not go so far as to say that expert testimony is of no weight here. Some of it we have found interesting and even instructive. But in view of the nature of the issues raised, we think its weight limited. We note, for example, that some of the experts seem to have spent a great deal of time studying our decisions under Section 17 of the Act and pondering the implications of the opinions in those cases. That sort of thing is normally the function of a lawyer, not of an expert witness. The Division has, we think, failed to give due heed to the special nature of this concrete case. Observations about experts in our past opinions have been mechanistically transposed to contexts quite different from those in which they were uttered.

merger cannot possibly do as much for Du Pont as it will for Christiana. The very slight reduction in the amount of Du Pont's outstanding common and the resulting increase in earnings per Du Pont common share is incommensurate with the tax and the market value benefits inuring to the Christiana stockholders.

Applicants ask us to look at other benefits that will, they say, be reaped by Du Pont and its stockholders. We have done that. And we find their magnitude far from striking.

Apart from the small reduction in the number of Du Pont shares outstanding and the resulting small increases in book value and in earnings per Du Pont common share, it is said that Du Pont will benefit from:

(A) The "dispersal" of Christiana's large block of Du Pont common; and

(B) Its escape from the Investment Company Act, which precludes it from entering into transactions with Christiana without our approval.

The "dispersal" argument is somewhat puzzling. Applicants insist over and over again that it is most unlikely that any substantial number of Du Pont shares will come to market by reason of the proposed transaction. In that regard applicants point quite cogently to the large individual capital gains taxes that selling Christiana holders will have to pay and to the long-run character of the du Pont family's investment commitment to the company that bears its name. What then is likely to be dispersed?

It would seem that the dispersal will be formal, not substantive. Today some people own a great deal of Du Pont indirectly through Christiana. Tomorrow

those very same people will still own a great deal of Du Pont. But they will own it directly rather than indirectly. What will that change do for Du Pont?

Du Pont's answers to these questions look to the long run. Its brief concedes that its "management was aware of no immediate prospect of any adverse consequences from the Christiana holdings." The brief goes on to argue, however, "that over the long term such a possibility might arise."

The precise nature of these possible long-term adverse consequences is obscure. The argument rests on the possibility of a future clash between the people then in control of Christiana and the people then managing Du Pont. It assumes that in this hypothetical situation the Du Pont managers will be the "good guys" and the Christiana control group the "bad guys." The argument seems far-fetched and rests on premises we consider unacceptable. Christiana's extinction may well make it somewhat easier for Du Pon't managers to maintain themselves in office. We, however, cannot presume that this will necessarily be in the Du Pont stockholders' interest.[39] And in any event the Investment Company Act was not designed to foster the retention of control by managerial groups. Nothing in it warrants a holding that such control is to be preferred to control by important stockholders.[40]

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[39] As a former Chairman of this Commission recently observed: "The raider may . . . be a better manager than the raidee." Cary, *A Proposed Federal Corporate Minimum Standards Act*, 29 BUS. LAW. 1101, 1105 (1974).

[40] Certain Delaware decisions seem to hold otherwise. They are beside the point. Our concern here is not with the niceties of local corporation law, but with broad Federal investor-protection standards formulated in large measure because of the inadequacies of

No showing has been made that the Investment Company Act imposes any really onerous burdens on Du Pont. No doubt the applications that the company is required to file by reason of its affiliation with Christiana are something of a nuisance.[41] But no contention has been made that the Act has interfered or is likely to interfere with the company's business. Hence we find it is difficult to view Du Pont's exit from the Act's net as a significant benefit.

But the Act's requirement that the transaction be reasonable, fair, and free from overreaching, does not mean that the benefits to the parties must be nicely balanced. Such a reading would be wholly impractical and would frustrate legitimate arrangements. Some transactions are more important to one side than to the other. This one is of that type. And that does not make it inherently unfair under Section 17(b). Nor does the fact that Christiana has much more at stake than Du Pont mean that the consideration moving from Christiana to Du Pont must be large enough to inflict really substantial detriment on the former.

The benefit to Du Pont is far from awesome. But it is sufficient to meet the statutory standard. Christiana is a legal device. Those who invented it did so to serve their own purposes.[42] And they had every right to do

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local corporation law. See Cary, ***Federalism and Corporate Law*: *Reflections upon Delaware*,** 83 YALE L.J. 663 (1974).

[41] Our files show that there have been approximately 50 applications since the Investment Company Act went into effect back in 1940.

[42] The parties did not go into Christiana's history on the record. But we thought it appropriate to take administrative notice of some fairly well-known facts of economic history. And we did so at the outset of this opinion. We cannot forget that Christiana as an

that. Now the inventors' heirs and successors in interest conclude that the device is obsolete. That is their privilege. Nothing in the Act compels them to pay a high price for exercising it.[43] Only if their decision to

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investment company is of a very special kind and that the situation with which we are confronted was created long, long before anyone dreamed of any such statute as the Investment Company Act. Compare *Hawaiian Electric Company, Inc.*, Holding Company Act Release No. 16592 (January 26, 1970), p. 5 where our view of the Public Utility Holding Company Act's impact on the matters there before us was much influenced by Hawaii's unique history.

The Public Utility Holding Company Act to which we have just referred has a certain bearing here. As applicants note, Section 11(b)(2) of that statute mandates the elimination of unnecessary holding companies in the industries affected. Were that Act applicable to Christiana, it would have vanished long ago. Nobody suggests that it serves any real purpose in the world of today. Of course, Du Pont is neither an electric company nor a gas company. So we have no power to destroy Christiana on our own motion. But we think the policy against the multiplication of superfluous corporate entities articulated in the Holding Company Act sound and salutary. When as here questions about wholly unnecessary entities come before us in non-utility contexts, it is quite inappropriate for use to insist on their perpetuation or to impose terms likely to lead the parties to conclude that it would be cheaper and better to keep them alive.

[43] But they must pay a fair price. And in assessing the fairness of the proposed price one is struck by the fact that the Securities Act restricts the marketability of Christiana's massive block of Du Pont. Objectors do not demur to the proposal on this ground. Nor does our staff. We, however, have considered the question *sua sponte*. We have done so because (1) as the Commission pointed out some years ago, "the valuation of restricted securities at the market quotations for unrestricted securities of the same class would, except for most unusual situations, be improper." (*"Restricted Securities,"* Investment Company Act Release No. 5847, Accounting Series Release No. 113 (October 21, 1969)); and (2) in the normal case a discount of only 2.5% from net asset value would be much too small to reflect the diminution in value resulting from the restrictive feature. After such consideration, we find this one of those "most unusual situations" referred to in the above-

dismantle Christiana inflicts cognizable harm on Du Pont and on its stockholders unrecompensed by the

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cited release in which it is proper to value restricted securities at the price assigned by the market to unrestricted securities of the same class.

The typical investment company-restricted security situation involves the acquisition of a block of restricted securities for investment at a price below that at which unrestricted securities of the same class are selling, with the discount (usually a substantial one) being attributable to the restrictions imposed by the Securities Act on persons who take securities in so-called private placements. None of these factors is present here. Christiana's 13,417,120 shares of Du Pont were not acquired for investment in the ordinary sense of that term. Those shares are a historic control block assembled almost two decades before anyone thought of any such statute as the Securities Act. And although the price Christiana paid for its Du Pont holdings was nominal when viewed in relation to their present value, it received no discounts at the time of purchase. What has just been said is more than historical digression. It has contemporary relevance. A block of securities restricted under the Securities Act because it is large enough to confer control cannot be equated mechanically for all purposes with smaller non-controlling blocks restricted only because they were acquired in transactions claimed to have been exempt from the Securities Act's registration and prospectus-delivery requirements by reason of the special provision in Section 4(2) of that statute for "transactions . . . not involving any public offering." Our policy with respect to the valuation of restricted stock by investment companies rests on two principal considerations. First, the impropriety of an investment company recording essentially fictitious profits by buying restricted stock at a discount and then marking it up to the market; and secondly, the fact that stock which cannot be publicly sold without registration normally is worth less than stock which is free for trading. Neither consideration is applicable here. Christiana did not acquire DuPont stock at a discount by reason of the status of that stock under the Securities Act, and Christiana never intended to, and never has, traded in and out of DuPont stock. If Christiana had ever made the clearly momentous decision to attempt to sell its DuPont stock, registration under the Securities Act would have been the least of its problems.

Also pertinent in this regard is the fact that much (probably

proposed discount, can we insist on terms harsher for them than those now before us.[44]

Another aspect of this case illustrates that principle. The Christiana stockholders could have caused Christiana to be liquidated. They would then have become

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most) of the Du Pont stock to be received by the Christiana stockholders will itself be restricted under the Securities Act. To discount the value of those persons' present indirect holdings in Du Pont on the ground that those holdings are restricted under the Securities Act and then to give them new direct Du Pont shares that would be similarly restricted, would involve a double subtraction that we deem impermissible.

[44] It might seem that the discount should at the very least equal the 7.2% income tax benefit to be realized by the Christiana stockholders. However, their actual benefit will in most cases be less than 7.2%. See p. 10, *supra*. This consideration, however, we put to one side. The heart of the matter is that the tax benefits to be reaped by the Christiana people will inflict no corresponding detriment on Du Pont or on its stockholders. The burden will fall wholly on the United States. And neither the du Pont family nor the other Christiana holders are under any duty to maximize their tax liabilities. As the Court of Appeals for the Second Circuit said when it spoke through Judge Learned Hand in *Helvering* v. *Gregory*, 69 F.2d 809, 810 (1934): "Anyone may so arrange his affairs that his taxes shall be as low as possible; he is not bound to choose that pattern which will best pay the Treasury; there is not even a patriotic duty to increase one's taxes." Also in point are Judge Hand's subsequent observations when he dissented in *Commissioner* v. *Newman*, 159 F.2d 848 (C.A. 2, 1947), *cert. denied* 331 U.S. 859 (1947): "[T]here is nothing sinister in so arranging one's affairs as to keep taxes as low as possible. Everybody does so, rich or poor; and all do right, for nobody owes any public duty to pay more than the law demands: taxes are enforced exactions, not voluntary contributions. To demand more in the name of morals is mere cant." 159 F.2d at 850-851. Nor do we see how Section 17(b)'s "reasonable and fair" standard can be deemed to require Christiana's stockholders to turn every nickel of their tax savings over to Du Pont. The tax savings are of some weight. But it does not follow that the Du Pont stockholders are to be subrogated to the rights that the United States now enjoys under the status quo.

the direct owners of the Du Pont shares now held by Christiana. Had they done so, the situation would have been essentially the same as that contemplated by this merger.

But a liquidation, unlike this merger, would have adverse tax consequences for Christiana's stockholders. And in view of the problems attributable to the General Motors divestiture, the extent of their potential tax liability is shrouded in uncertainty.[45] The proposed merger is thus designed to avoid the serious tax problems that Christiana's liquidation would engender for its stockholders. Aside from those tax problems, however, the economic impact of this merger on Du Pont and its stockholders is no more onerous than the impact that would be produced were the Christiana stockholders to exercise their prerogative to liquidate Christiana. More specifically, the possible market effects resulting from the Christiana stockholders acquiring direct ownership of the Du Pont shares would be the same. It may be that in the course of bargaining between wholly unrelated parties, Du Pont could have exacted a handsome price for permitting consummation of the transaction in a form that relieves the Christiana stockholders of their tax problems. But Du Pont's failure to do that does not render the transaction unreasonable or unfair. The Du Pont stockholders, including the objectors, have no property interest in the Christiana stockholders' tax problems. A principal reason why Section 17 of the Investment Company Act requires us to pass upon the fairness of transactions such as this, is to prevent persons in a

[45] See n. 31 on pp. 10-11, *supra*.

strategic position from using that position to effect transactions for other than fair value. And fair value does not change simply because a strategic position arises from something other then affiliation.

X

That brings us to what we think the crux of the case: the objectors' claim of detriment by reason of market impact.

Here we find a hot dispute about the probable facts. Objectors envision endless torrents of Du Pont shares descending on the market. Although never too clear about exactly what they expect to happen, they profess great alarm about the low prices to which Du Pont common will fall.[46] Applicants laugh at that. They say

[46] But they never explain why Christiana's holders would be eager to sell at such depressed levels. Objectors have no doubts about Du Pont's investment merit. Indeed, they think Du Pont a pearl of great price. Nor do they suggest that those who guide Christiana's destinies have any real doubts about Du Pont. The objectors' position is self-contradictory. On the one hand, they stress the great wealth of the du Ponts. On the other, they are (or claim to be) obsessed by the virtual certainty of massive sales at distress prices. But why should people whose remoteness from the brink of destitution is constantly stressed by the objectors themselves rush off madly to dispose of valuable property for less than its intrinsic worth? Objectors never answer that question. Instead they shift their ground by moving from the Christiana control group to the non-controlling public investors who own about 25% of Christiana. These people, they note, will be free from the Securities Act's registration and prospectus-delivery inhibitions. They proceed to postulate devastating waves of helter-skelter selling by the public holders. These horribles seem fanciful to us. We see no reason to assume that there will be a psychosis epidemic among either the controlling or the non-controlling Christiana stockholders. We think that in financial matters at least both groups are at least as rational as the general run of Humanity.

that nobody is going to sell anything. Christiana's brief tells us that:

> "In the present situation, there is no reason to suppose that the distribution of Du Pont shares to Christiana stockholders will add even one share to the market for Du Pont stock. The consummation of the merger will simply leave the Christiana stockholder with Du Pont shares in place of the Christiana shares he has formerly held—in most cases—for many years. There is no reason to suppose that the Christiana stockholder will sell those shares . . . [A]dverse tax consequences will be visited on a former Christiana stockholder if he does see Du Pont stock. Those consequences are a strong deterrent to sale since receipt of the Du Pont stock in the merger will be tax-free."

We think the objectors' prophecies much too gloomy.[47] Hence it looks to us as though the applicants have the better of the argument. But we refrain from enmeshing ourselves in this thicket of conjectures about what people are likely to do in the future with their own property.

We assume that the merger may engender some selling that would otherwise not take place. We assume further that such selling may at certain points in time be substantial. Proceeding on those assumptions, we are nevertheless after considerable thought unable to detect any uncompensated detriment to the Du Pont stockholders of a type that we can properly take into account.

The stock market has its peculiarities. In essentials, however, it is much like other more basic markets in

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[47] Our reasons have been stated in the preceding footnote.

goods, services, and the factors of production. Here as elsewhere increased supply will (all other factors being equal—which in practice they may or may not be) lower prices. Should the Wilmington Trust Company decide to sell a substantial amount of Du Pont common, the price of the issue will be affected to some extent.

We agree with the objectors about that. But we disagree with their contention that this short-run view of the pricing process is the one that governs here. What we have before us in these proceedings is a proposal for a fundamental corporate readjustment. In that context transitory market phenomena are of secondary significance. We look at the case not from the objectors' tape-watcher perspective,[48] but as a problem in economic realities and business fundamentals.[49]

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[48] We cast no aspersions on tape watchers. They have every right to speculate. And while pursuing their own self-interest, they sometimes perform a useful social function. Hence they are often the objects of our solicitude. But that is so in matters arising under the Securities Exchange Act. When we work under this Act, under Chapter X of the Bankruptcy Act, and under the Public Utility Holding Company Act, their interests yield to those of the long-term investor.

[49] We may draw attention to what we consider the striking parallel between Section 17(b)(1)'s reasonable, fair, and free from overreaching test and the "fair and equitable" standard that Congress laid down in the Bankruptcy Act (Sections 174, 221(2)), and in the Public Utility Holding Company Act (Section 11(e)). True it is that the words "fair and equitable" have a precise technicial meaning in insolvency law. Nor are we unmindful of the distinctions that may well be drawn between a legally mandated reorganization under the Holding Company Act and a consensual arrangement such as the one now before us. But the ancient reorganization concept of "fair and equitable" also has a broader meaning that we think indistinguishable from the Investment Company Act

Hence we find ourselves compelled to discount objectors' market impact worries even more heavily than they would have us discount Christiana's net asset value. A share of Du Pont common is a fractional proprietary interest in a large business. In no way will the Christiana merger detract from either the assets or the earning power of that business. The fundamentals of the situation will remain as they are. Thus the merger cannot affect—and no contention has been made that it would or could affect—Du Pont's intrinsic investment value. That the merger might

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test that governs here. See *Protective Committee* v. *Anderson,* 390 U.S. 414, 424-441 (1968).

Hence we find the many reorganization cases that emphasize intrinsic value and deprecate market factors persuasive here. See, e.g., *S.E.C.* v. *Central-Illinois Securities Corp.,* 338 U.S. 96, 152 (1949) ("Congress, perhaps believing that the application of such an amorphous standard as that of 'colloquial equity' was beyond the competence of courts and commissions, has instead prescribed the requirement that investment values be preserved."); *Niagara Hudson Power Corp.* v. *Leventritt,* 340 U.S. 336, 346-348 (1951) ("The informed judgment of the Commission, rather than that of the market, has been designated by the Act as the appropriate guide to fairness and equity within the meaning of the Act. Under the standards approved by this Court, that informed judgment looks for investment values. . . . [T]he *Central-Illinois* case . . . expressly rejected the 'colloquial equity' approach of the District Court, which placed special emphasis upon market history. . . . Moreover, we find no lack of authority . . . [for] the general principle that a class of securities may go unrecognized in a reorganization when . . . they have no investment value.") Pertinent here are the District Court's observations at the close of its opinion in *In re Imperial '400' National, Inc.,* 374 F. Supp. 949, 978 (D.N.J., 1974): "Concern has been expressed . . . with respect to the market value of new . . . stock as opposed to its investment value. No matter how carefully I may calculate 'value,' I have no control over what may happen to price in the public market. But my concern under the Bankruptcy Act is value and not price."

possibly engender selling of a volume that could on occasion cause Du Pont's market price to dip below the level at which it would otherwise stand is of little moment. Such undervaluation would undoubtedly attract the attention of investors and speculators interested in chemical issues. They could scarcely escape noticing it. And why would they spurn the resulting bargain? Nothing brought to our attention suggests that the marketplace might be slow to notice Du Pont's cheapness relative to comparable stocks. And we see no reason to assume that it would. We therefore conclude that such depressing effects on the price of Du Pont common as may occasionally manifest themselves by reason of the proposed transaction will be of relatively brief duration. We proceed on the premise that over time the securities markets are rational.[50] And if that premise be sound, an issue as well-known and as conspicuous as Du Pont common cannot remain on the bargain counter for long.[51]

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[50] The premise may or may not be empirically demonstrable. Some academicians who speculate about the nature of speculation question it. But see the observations on "central value" and "intrinsic value" in GRAHAM, DODD & COTTLE, SECURITY ANALYSIS 26, et seq. (4th ed., 1962). We, however, are not at liberty to question it. The statutes we have been directed to administer start from the axiom that markets are or can be made economically rational. We are no freer to question that axiom than we are to question the desirability of registration statements and prospectuses under the Securities Act. If prices and values are as unrelated to each other over time as the objectors contend, the Investment Company Act is nonsensical and this Commission's labors under it farcical. For obvious reasons we take a different view.

[51] The closed-end discount that pervades this case may raise doubts about this. The closed-end discount phenomenon, which is neither peculiar to Christiana nor of recent vintage (see our previously cited 1966 report on the PUBLIC POLICY IMPLICATIONS

Suppose that we were inclined to see more abstract merit than we do in the objectors' market impact argument. Even then we would be unable to give it much weight in deciding the concrete case before us. How can we possibly tell how much Du Pont common is likely to come to market by reason of this merger in 1976? 1980? 1985? And even if we could form some educated guesses about that, how would we measure the impact of the additional supply on the market price? The objectors are unable to supply us with supply and demand schedules for Du Pont common for the ensuing decade.[52] And we decline to construct our own.[53] Speculations about the probable behavior patterns of speculators are much too slender a reed on which to predicate findings of fairness under the Investment Company Act.[54]

OF INVESTMENT COMPANY GROWTH at pp. 42-44; see also Metz, *Unkindly Year in Closed Ends*, N.Y. Times, January 11, 1974 at 42, col. 3; *Where Stocks Can Be Bought at a Discount*, U.S. NEWS & WORLD REPORT, May 27, 1974, p. 61) has its intriguing and to some extent disquieting aspects. But we see nothing in it that serves as an augury about the probable market action of a stock like Du Pont. Closed-end companies are seldom liquidated. Investors attracted to them by the discount assume the risk that the discount may widen against them. And in Christiana's case special factors come into play. Du Pont is an active, well-known listed stock. Christiana, on the other hand, is a thinly traded over-the-counter issue. The *relative* illiquidity of an investment in Christiana would seem to have had some influence on the discount.

[52] Were there any such schedules, their very existence would alter the situation. If investors and speculators had the benefit of perfect foresight, they would alter their plans.

[53] Having denounced investment advisers who "vie with each other in making unsupportable claims to prophetic insight" (*Spear & Staff, Incorporated*, 42 S.E.C. 549, 556 1965)), we refrain from similar transgressions of our own.

[54] Compare *Jade Oil & Gas Co.*, Corporate Reorganization Release No. 289, p. 14 (September 15, 1969).

Even if we had the light of hindsight available to us, we could not properly focus on the factors the objectors consider central.

Suppose that we were able to take another look at this case some years after the merger. Du Pont's actual post-merger market history would then be available to us. But it would be of little help. Stock prices are volatile and the factors that influence them multifarious.[55] We know of nothing that would permit an accurate post-merger assessment. A pre-merger one would obviously be an even wilder guess.

XI

At times the law undertakes explorations almost as speculative as those on which the objectors ask us to embark. Thus in the law of tort judges and juries place price tags on pain and suffering—and indeed on human life itself. And to come closer to home, in reorganizations under the Bankruptcy and Public Utility Holding Company Acts we and the courts try to estimate the probable future earnings of business enterprises and the multiples at which it is appropriate to capital-

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[55] Du Pont is generally regarded as an issue of prime investment quality. Applicants and objectors agree on that. Yet during 1974 its price has ranged from 179 to 84½. Lest 1974 be tossed off as an especially disturbed year, we look for comparative purposes to 1970-1972. And we find that during those years the price ranged from 184 to 92. Du Pont is now selling at 8 times earnings. Not too long ago it was selling at 24 times earnings. Some years ago it was at 27 times earnings. These numbers show the inherent futility of any effort to measure the impact of incremental supply. Yet objectors ask us to assess the psychological effects of purely potential supply.

ize those earnings.[56] Those inquiries are undertaken because justice requires that the effort be made.

That differentiates those situations from this one. Here justice requires no ventures into the unknown and unknowable. An investment company, whose assets consist entirely or almost entirely of securities the prices of which are determined in active and continuous markets, can normally be presumed to be worth its net asset value. What better guide to its value could there be? The simple, readily usable tool of net asset value does the job much better than an accurate gauge of market impact (were there one) could. The record indicates that most of Christiana's stock is held by long-term investors. Hence there is no pressing need to depart from the net asset value test.[57]

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[56] See *Consolidated Rock Products Co.* v. *Du Bois,* 312 U.S. 510, 526 (1941) quoted with approval in *Protective Committee* v. *Anderson,* 390 U.S. 414, 441-442 (1968): "The criterion of earning capacity is the essential one. . . . Since its application requires a prediction as to what will occur in the future, an estimate, as distinguished from mathematical certitude, is all that can be made."

[57] Investment companies are as a general rule media for long-term investment. That makes net asset value the touchstone. And the Act is based on that premise. Section 2(a)(41)(B) states that " 'Value' with respect to assets of registered investment companies . . . means . . . with respect to securities for which market quotations are readily available, the market value of such securities." And although the closed-end discount phenomenon was well-known in 1940, the Congress that passed the Act chose to protect closed-end stockholders against dilution of intrinsic values rather than to facilitate the sale of new closed-end shares. Section 23(b) of the Act shows that. It provides that "No registered closed-end company shall sell any common stock of which it is the issuer at a price below the current net asset value of such stock." And we have viewed net asset value as the controlling factor in Section 17 proceedings. See, e.g., *Harbor Plywood Corporation,* 40 S.E.C. 1002, 1010 (1962); *Delaware Realty and Investment Company,* 40 S.E.C. 469, 473

That understates matters. In these circumstances, any significant departure from the net asset value criterion would work positive injustice. Objectors' proposals would strip the long-term Christiana investor of some of the intrinsic value of his holdings. Such expropriation would be wholly unjustifiable. It would also be most inappropriate to frustrate the reasonable expectations of those who bought into Christiana in the belief that it was a legitimate way of buying Du Pont at a lower price.[58]

XII

Having concluded that pecuniary assessment of hypothetical future market impact would be unnecessary and inappropriate,[59] we turn to the objectors' sugges-

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(1961). Compare *Central States Electric Corporation*, 30 S.E.C. 680, 700 (1949) (advisory report on plans for the reorganization of a closed-end investment company under Chapter X of the Bankruptcy Act urging "net asset value as the primary measure of value of an investment company.")

[58] Objectors talk of windfalls. We cannot detect them. True, people bought Christiana on the theory that it was a cheap way of buying Du Pont. But those who did that took the risk that the closed-end discount might widen against them. Those who reasoned that long-run value would win out in the end and that Christiana could not last forever will do well. But such rewards for astuteness and lucky guesses are inherent in the nature of markets.

[59] Objectors make much of certain assertedly contrary positions said to have been taken by the applicants, their controlling persons and their counsel and financial advisers in the Du Pont-General Motors divestiture proceedings. See *United States* v. *E. I. du Pont de Nemours & Co.*, 353 U.S. 586 (1957); 177 F. Supp. 1 (N.D. Ill., 1959); 366 U.S. 316 (1961). But the views that the applicants found it convenient to take in another case under another statute before another forum are not controlling here. Moreover, the General Motors situation had nothing in common with this one. There Du Pont was to distribute its millions of General Motors shares to

tions for restraints on the alienation of the Du Pont shares to be issued under the merger.[60]

The Securities Act is now 41 years old. Hence there is nothing novel about the idea that it is in the public interest and appropriate for the protection of investors to inhibit certain strategically situated persons from selling securities whenever and wherever they choose. But neither the Securities Act nor the Securities Exchange Act prohibits such people from selling. What those statutes prohibit are offers and sales without appropriate disclosure. It is a long, long jump from that to an unconditional ban on any sales at all. And quantitative limits on a holder's freedom of sale that rest not on the buyers' need for disclosure, but on the assumed desirability of protecting other holders from the market effects of large-scale selling would entail almost as broad a leap. We see no need for such a leap in this case.[61]

Du Pont's stockholders. Under the Internal Revenue Code, as it then was, the recipients of those shares would have been deemed to have realized taxable income. So they would have had to pay taxes. To raise the money with which to pay those taxes, they would or might have had to sell at least some of the General Motors shares that they received by reason of the divestiture. (This problem was solved for the most part by the addition of Section 1111 to the Internal Revenue Code.) Here no taxes need be paid except by those Christiana holders who may voluntarily decide to sell. Nor are the governing legal standards the same. The Internal Revenue Code's standard is "fair *market* value." The word "market" is conspicuously absent from Section 17(b).

[60] No specific suggestions are made.

[61] Objectors seek to protect their property rights. But the Christiana stockholders also have property rights. It is not for us to prefer one group's property rights over the other's. The Du Pont stockholders are far more numerous than the Christiana stockholders. See n. 34 on p. 11, *supra*. But that is of no consequence.

XIII

We said earlier that this is not an easy case. But its difficulties do not stem from the hypothetical market impact on which objectors focus. They flow rather from the striking disparity between the substantial benefits to be received by Christiana and the far more modest ones inuring to Du Pont. This disparity justifies the proposed 2.5% or 1.8% discount from Christiana's net asset value. That is not to say that applicants have come up with *the* one right figure. There is no such figure. Fairness is a range, not a point. Something less than the discount arrived at by the applicants might well pass muster.[62] And a slightly higher dis-

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These matters are not resolved by plebiscite. Section 17(b)(1) seeks to prevent "overreaching on the part of any person concerned." Compare *Protective Committee* v. *Anderson,* 390 U.S. 414, 435 (1968): "[A] plan of reorganization which is unfair to some persons may not be approved by the court even though the vast majority of creditors have approved it."

[62] Objectors say that the applicants' negotiations were not at arm's-length. And in view of the links between Christiana and Du Pont they may well be right about that. It matters not. In assessing fairness we look not to the nature of the negotiations but to their results. It is precisely because transactions of this character are replete with inherent conflicts of interest that the Act requires that they be submitted to us. As we said in *Atlas Corporation,* 37 S.E.C. 72, 85-86 (1956): "It is evident that Section 17 of the Act was not designed to prohibit transactions solely for the reason that they are not negotiated at arm's-length. On the contrary, Section 17(b) of the Act directs us to exempt transactions between controlling or affiliated persons where the evidence establishes that the terms thereof are reasonable and fair and do not involve overreaching on the part of any person concerned. Clearly, Section 17 contemplates that transactions meeting these standards will be permitted although arm's-length bargaining may not have been present or, indeed, may have been impossible in view of the relationship of the parties."

count would also be within the permissible range. But one appreciably higher than the discount now before us would divest Christiana's stockholders of a significant portion of the intrinsic investment values to which they are legally and equitably entitled. It would therefore run afoul of Section 17(b)(1) of the Act.[63]

XIV

We find the proposed merger:

(A) Reasonable and fair:

(B) Free from overreaching on the part of any person concerned;[65] and

(C) Consistent with the general purposes of the Act.[66]

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[63] That being our view of the law of the case, we see no merit to the objectors' contention that the record is so inadequate on the market impact aspect of the matter as to require a remand. Nor do we see any basis for the claim that adequate discovery about the Christiana control group's present intent to sell or refrain from selling in the future was improperly denied. To have delved into the matters into which objectors sought to inquire would have swelled the record pointlessly. Moreover, our Rules of Practice make no provision for the taking of depositions in situations other than those covered by Rule 15(a) of those rules. There may be a trend toward liberality in pre-trial discovery. But that did not empower the administrative law judge to disregard the plain meaning of our rules. Due process does not require depositions. See *Miner* v. *Atlass,* 363 U.S. 641 (1960); *N.L.R.B.* v. *Interboro Contractors, Inc.,* 432 F.2d 854, 857-858 (C.A. 2, 1970), *cert. denied,* 402 U.S. 915 (1971).

[65] We make no findings under Section 17(b)(2), which requires that the proposed transaction be consistent with the investment company's policy. That section has no bearing on cases in which investment companies propose to go out of existence. See *Aviation and Transportation Corporation,* 8 S.E.C. 527, 538-539 (1941).

[66] That is so because it will eliminate pyramiding duplicative operating expenses, and unnecessary taxation. See the *Aviation*

The standards of Section 17(b) being met, there is no need to invoke Section 6(c).[67]

An appropriate order will issue.

By the Commission (Chairman GARRETT and Commissioners LOOMIS, EVANS, SOMMER and POLLACK).

George A. Fitzsimmons
Secretary

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and Transportation case cited in the preceding footnote, at page 539 of 8 S.E.C.

[67] Applicants also pray for exemptive relief from Section 17(d) of the Act and our Rule 17d-1 thereunder. No issue has been raised as to the applicability of those provisions. Hence we assume without so deciding that they may have some bearing here. To the extent, if any, that this is so, we find the standards of that section and that rule satisfied.

United States of America
before the
Securities and Exchange Commission

Investment Company Act of 1940
Rel. No. 8615/December 13, 1974

Admin. Proc. File No. 3-3928

In the Matter of

Christiana Securities Company
Wilmington, Delaware

E. I. Du Pont de Nemours and Company
Wilmington, Delaware
(812-3224)

Order Granting Application

Christiana Securities Company, a registered closed-end non-diversified investment company, and E. I. du Pont de Nemours and Company, its affiliate, made joint application under Sections 17(b) and 6(c) of the Investment Company Act for an exemption from Section 17(a) of certain transactions incident to a merger of Christians into Du Pont. The application also sought permission to effect such transactions under Section 17(d) and Rule 17d-1.

Hearings were held after appropriate notice. An initial decision by the administrative law judge was waived. Proposed findings and briefs were filed. And the Commission heard oral argument.

The Commission has this day issued its Findings and Opinion. On the basis of such Findings and Opinion, it is

ORDERED that the proposed transactions be, and they hereby are, exempted from Section 17(a) of the Investment Company Act; and it is further

ORDERED that said transactions be, and they hereby are, exempted from Section 17(d) of that Act and from Rule 17d-1 thereunder.

By the Commission.

George A. Fitzsimmons
Secretary

APPENDIX B

INVESTMENT COMPANY ACT OF 1940
Release No. 8692/February 27, 1975

Admin. Proc. File No. 3-3928

In the Matter of

CHRISTIANA SECURITIES COMPANY
Wilmington, Delaware

E. I. DU PONT DE NEMOURS AND COMPANY
Wilmington, Delaware

(812-3224)

MEMORANDUM OPINION AND ORDER DENYING REHEARING AND LEAVE TO ADDUCE ADDITIONAL EVIDENCE.

I.

The objecting shareholders whose contentions were rejected in Investment Company Act Release No. 8615 (December 13, 1974), 5 SEC Docket 745 seek rehearing. But their petitions raise nothing of substance that is new.[1] Nor do they convince us that our original decision was wrong.

[1] That is so even though the principal petitioner received an unprecedently generous extension of time to enable him to perfect his petition. He told us that such extension was needed because of the complexity of the case. Agreeing that an extension was appropriate, we granted his request over the applicant companies' strenuous objections.

II.

One objector also asks for leave to adduce additional evidence. That consists of:

(A) Seven specifically identified documents that could, he suggests, "aid . . . a court on review and . . . help them [sic] visualize the factual situation and various publicized statements and the interrelationships"; and

(B) Unspecified materials said to have been discovered in a pending shareholder's derivative action.

Petitioner does not contend that the identified documents are material.[2] As already noted, he states only that they might "help" a reviewing court to "visualize the factual situation." But how would they do that? Petitioner doesn't say.[3]

The unidentified evidence said to have been gathered in the derivative action goes to petitioner's market impact contentions. Petitioner wants to show that the

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[2] They consist of three notices of annual meetings, a proxy statement with respect to one of those meetings, one of Christiana's semiannual statements, a report by Christiana to use on our Form N-1R, and another company's annual report. Four of these documents were available when the hearings were held. Petitioner claims to have discovered "most of this material" after the close of the hearings herein. But in view of their nature and ready accessibility it seems to us that petitioner would have learned of these papers earlier—had he been reasonably diligent. Most of the documents are in our public files and hence available to anyone who wants to look at them.

[3] With respect to only a single document, does the petitioner state what he wants to show through it. He says in effect that it shows that the applicant companies are under common control. We have already held that this is so. Release at p. 6, 5 SEC Docket at 752.

proposed merger will lead to massive sales of Du Pont's common stock and that this *"goes right to the fairness issue."* (Emphasis his.) But we have already said in our opinion that: "We assume that the merger may engender some selling that would otherwise not take place. We assume further that such selling may at certain points in time be substantial.[4] So petitioner wants to adduce additional evidence in support of a hypothesis that we have already accepted on the record as it stands. No showing has been made that such additional evidence would serve any useful purpose.

Petitioner's argument that the projected selling "goes right to the fairness issue" is legal, not factual. We rejected that argument because we think such selling irrelevant to the fairness issue framed by the Investment Company Act. That holding does not turn on evidentiary details. It rests on our reading of the Act.[5] Hence additional evidence cannot alter the result.[6]

We conclude that the instant application does not meet the test precribed by Rule 21(d) of our Rules of Practice, which requires that an application for leave to adduce additional evidence "show . . . that such additional evidence is material and that there were

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[4] Release at p. 19, 5 SEC Docket at 750.

[5] In footnote 38 to our opinion (Release at p. 14, 5 SEC Docket at 754) we said that "The questions presented are in our view essentially legal."

[6] Petitioner recognizes this. He says in his petition: "Reading the opinion of the Commission leaves the impression that there is no fact question that could move the Commission to abandon the legal rulings which seem to preclude and indeed preempt factual issues . . . there is little that can be done by way of evidence."

reasonable grounds for failure to adduce such evidence . . . before . . . the hearing officer."[7]

III.

Accordingly, IT IS ORDERED that the petitions for rehearing and the petition for leave to adduce additional evidence be, and they hereby are, in all respects denied.

By the Commission (Chairman GARRETT and Commissioners LOOMIS, EVANS, SOMMER and POLLACK).

George A. Fitzsimmons
Secretary

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[7] *Cf. Gross* v. *SEC*, 418 F.2d 103, 108 (C.A. 2, 1969).

APPENDIX C

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

No. 75-1100

RICHARD J. COLLINS, JR.,
PETITIONER,
v.
SECURITIES AND EXCHANGE COMMISSION,
RESPONDENT.

No. 75-1262
No. 75-1263

LEWIS C. MURTAUGH, TRUSTEE FOR EMANUEL AND HELEN STEIB, UNDER DECLARATION OF TRUST DATED 8/30/56,
PETITIONER,
v.
SECURITIES AND EXCHANGE COMMISSION,
RESPONDENT.

PETITIONS FOR REVIEW OF ORDERS OF THE SECURITIES AND EXCHANGE COMMISSION.

Submitted: September 10, 1975
Filed: January 23, 1976

Before HEANEY, STEPHENSON, Circuit Judges, and TALBOT SMITH, Senior District Judge.*

* TALBOT SMITH, Senior District Judge, Eastern District of Michigan, sitting by designation.

HEANEY, Circuit Judge.

We review an order of the Securities and Exchange Commission exempting from the prohibition of §17(a) of the Investment Company Act of 1940, 15 U.S.C. §80a-1 *et seq.*, the proposed merger of Christiana Securities Company into E. I. du Pont de Nemours and Company. The Commission granted the exemption after finding the merger terms to be reasonable and fair and free from overreaching on the part of anyone concerned within the meaning of §17(b)(1)[1] of the Act. We reverse because:

(1) The Commission's order is premised on the erroneous view that Christiana should presumptively be valued on the basis of the market value of its principal asset, common stock of Du Pont.

(2) The record as a whole does not support the Commission's finding that the terms of the merger are reasonable and fair and free from overreaching on the part of anyone concerned.

I. STATEMENT OF UNDERLYING FACTS.

Christiana is a closed-end, non-diversified management investment company[2] registered with the Com-

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[1] The Commission found the merger to be consistent with the general purposes of the Act. *See* 15 U.S.C. § 80a-17(b)(3). No appeal is taken from this finding. It made no finding with respect to § 17(b)(2) of the Act which requires a proposed transaction to be consistent with the investment company's policy because Christiana was proposed to go out of existence.

The Commission's decision is reported as *Christiana Securities Company*, Investment Company Act Release No. 8615 (December 13, 1974).

[2] *See* 15 U.S.C. § 80a-5.

mission pursuant to the Act. It was created in 1915 as a device by which members of the du Pont family could concentrate their large holdings in Du Pont and maintain control of that company.[3] The family members contributed their Du Pont stock to Christiana in exchange for Christiana shares. Christiana now holds 13,417,120 shares of Du Pont common stock, representing twenty-eight and three-tenths percent (28.3%) of the issue.[4] It has outstanding 11,710,103 shares of its common stock and 106,500 shares of its preferred stock. Seventy-five percent (75%) of Christiana stock is held by members of the du Pont family. Ninety-five and five-tenths percent (95.5%) of Christiana's stock

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[3] Christiana also owns a small block of Du Pont preferred stock, two daily newspapers in Wilmington, Delaware, and three and five-tenths percent (3.5%) of the stock of the Wilmington Trust Company. These holdings, representing two percent (2%) of its total assets, are not material to the issues on appeal.

[4] Members of the du Pont family who were directors of Du Pont or Christiana on December 31, 1971, owned an additional 426,876 shares of Du Pont common stock on that date. A request was made of the Commission by protester Murtaugh to inquire into additional stock ownership by the du Pont family. The request, in our view, was improperly rejected.

Christiana presumptively controls Du Pont. Section 2(a)(9) of the Act states: " 'Control' means the power to exercise a controlling influence over the management or policies of a company * * *." The presumption of control arises from the ownership of more than twenty-five percent (25%) of Du Pont's voting securities.

> There is little doubt that, for practical purposes, the block of common stock of E. I. du Pont de Nemours & Company, held by the Christiana Securities Company carries working control over the largest chemical company in the United States.

SEC, REPORT ON THE STUDY OF INVESTMENT TRUSTS AND INVESTMENT COMPANIES: CONTROL AND INFLUENCE OVER INDUSTRY AND ECONOMIC SIGNIFICANCE OF INVESTMENT COMPANIES, H. R. Doc. No. 246, 77th Cong., 1st Sess. (1941) at 152.

is held by three hundred and thirty-eight (338) holders of one thousand (1,000) or more shares each. The remaining four and five-tenths percent (4.5%) is owned by some seven thousand six hundred (7,600) shareholders.

Christiana's stock has historically sold at a discount from the market price of Du Pont common stock. Over the two years preceding the date on which the merger negotiations were announced, the discount generally ranged from twenty to twenty-five percent (20-25%). On the date of announcement, the discount was twenty-three percent (23%). The Du Pont stock owned by Christiana has a low or zero tax basis.

Du Pont is an industrial company principally engaged in manufacturing and selling diversified lines of chemical and other related products. It has 47,445,-810 shares of common stock outstanding, which are broadly and continuously traded on the New York Stock Exchange and other exchanges. These shares are owned by over 225,000 shareholders.

On April 20, 1972, Irénée du Pont, Jr., President of Christiana Securities Company, wrote to Mr. C. B. McCoy, President of Du Pont, suggesting a merger of Du Pont and Christiana.[5] As a result of this letter,

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[5] Dear Mr. McCoy:

As you know, Christiana Securities Company owns approximately 28% of the outstanding common stock of the Du Pont Company. In recent years this block of stock has represented about 99% of the total assets of Christiana.

We have believed over the years that Christiana has served a desirable and useful purpose in that it has tended to contribute to the continuity of sound and able management of the Du Pont Company. But there are certain disadvantages associated with the holding of such a large block of Du Pont stock in this form. For

negotiating committees were appointed by Du Pont and Christiana. Mr. McCoy, Chairman and President of Du Pont, and Irving Shapiro, Chairman of the Finance Committee of Du Pont, were named to represent Du Pont. Edward B. du Pont and A. Felix du Pont were named to represent Christiana Securities Company.

On June 6, 1972, the special negotiating committees jointly retained Morgan Stanley & Co., the Du Pont committee retained First Boston Corporation and the Christiana committee retained Kidder, Peabody & Co., Incorporated, as financial advisers. Each financial adviser was asked to recommend a range of terms for

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example, the market price for Christiana common stock consistently is lower than the value of the underlying net assets, Du Pont dividends flowing to Christiana are subject to Federal income tax at an effective rate of 7.2%, and there are certain conditions that limit to some extent the marketability of Christiana common stock. These disadvantages may now outweigh the benefits derived from the holding of a large block of Du Pont stock by Christiana, and a merger of Christiana with Du Pont could be desirable. Such a merger could also have advantages for Du Pont. I believe a merger might be practicable on terms that would be favorable to both Christiana and Du Pont and the stockholders of both companies.

Accordingly, I plan to call a meeting of the Board of Directors of Christiana for April 28, 1972 to discuss possibilities of a merger of Christiana into Du Pont. If the Christiana Board feels that such a merger might be desirable, I anticipate that a special committee of the Board will be appointed to develop possible terms for a merger.

I would appreciate your giving consideration to this matter from the standpoint of the interests of the Du Pont Company. If you feel that such a merger could be of possible interest to Du Pont, you might wish to appoint a special committee of the Du Pont Board to discuss the matter with a special committee of the Christiana Board appointed for such purpose.

Very truly yours,

Irénée du Pont, Jr.
President

exchange of Christiana common stock for Du Pont stock that was, in its opinion, reasonable and fair. Preliminary reports were made by the financial consultants at a joint meeting of the special committees on June 30, 1972. The final written reports were submitted on July 6 and 7, 1972. Each financial adviser recommended merger terms that approximated Christiana's net asset value.[6]

An agreement to merge was reached by the two negotiating committees on July 6, 1972, and approved by the Board of Directors of both corporations in principle on July 17, 1972. A formal plan of reorganization and agreement of merger was signed on December 20, 1972. The merger agreement provides for the issuance of Du Pont common stock equivalent in value to ninety-seven and five-tenths percent (97.5%) of Christiana's net assets after adjustments.[7] Each share

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[6] Morgan Stanley recommended terms ranging from a five-tenths percent (.5%) to a two and five-tenths percent (2.5%) discount from adjusted net asset value;

First Boston recommended a discount of between one and one-tenth percent (1.1%) and three and seven-tenths percent (3.7%) from adjusted net asset value; and

Kidder, Peabody recommended terms ranging from a two percent (2%) premium to a three percent (3%) discount from adjusted net asset value.

The Du Pont common stock was valued on the basis of its market quotations. This use of market price is not challenged on appeal.

[7] The adjustments reflected the following:

(1) Elimination of the claim for a tax refund, with provision for contingent delivery of Du Pont shares equivalent to the value of any refund;

(2) Allowance for expenses of sale and applicable capital gains tax on disposition of Wilmington Trust Company stock and The News-Journal Company; and

(3) Allowance for expenses of prosecuting the claim for tax refund and one-half of estimated merger expenses of $1,500,000.

of Christiana is to be exchanged for 1.123 shares of Du Pont. The preferred stock of Christiana can be converted into Du Pont common stock or redeemed pursuant to Delaware statutory procedures at $120 per share, plus accrued dividends. Common stock holders will also have appraisal rights under Delaware law.

Christiana and Du Pont submitted a joint application to the Commission for permission to merge on July 20, 1972. Notice of application was published on October 3, 1972. Thereafter, the protesters in this action and others filed a request for a hearing. A hearing was held before an Administrative Law Judge between February 5 to 13, 1973. The matter was argued in July, 1973. The Commission released its findings and opinion on December 13, 1974. It concluded that the statutory requirements as to reasonableness and fairness had been satisfied. The Commission subsequently denied the petitions filed by Messrs. Collins and Murtaugh seeking a rehearing and a petition by Murthaugh for leave to adduce additional evidence.

Collins filed a petition for review with this Court on February 7, 1975. Murtaugh filed a similar petition with the United States Court of Appeals for the Seventh Circuit on February 10, 1975. Murtaugh's petition was transferred to this Court pursuant to 28 U.S.C. §2112(a).

In reviewing the Commission's order, we are guided by the principle that the order is not to be disturbed unless it is predicated on an erroneous view of the law or is based on factual findings not supported by substantial evidence on the record as a whole. 15 U.S.C.

§80a-42(a); *Securities and Exchange Com. v. Chenery Corp.*, 332 U.S. 194, 207 (1947).

II. THE COMMISSION TOOK AN ERRONEOUS VIEW OF THE LAW.

We first turn to the question whether the Commission erred in holding, as a matter of law, that Christiana should be valued at the approximate value of its net assets (the market value of the Du Pont stock held by it). The Commission stated:

> An investment company, whose assets consist entirely or almost entirely of securities the prices of which are determined in active and continous [sic] markets, *can normally be presumed to be worth its net asset value.* What better guide to its value could there be? The simple, readily usable tool of net asset value does the job much better than an accurate gauge of market impact (were there one) could. The record indicates that most of Christiana's stock is held by long-term investors. Hence there is no pressing need to depart from the net asset value test. (Emphasis added.)

Christiana Securities Company, Investment Company Act Release No. 8615 (December 13, 1974) at 23.

This statement, which appears to state a rule of law rather than a rebuttable presumption,[8] was central to

[8] In view of the Commission's statement at n. 38 of its order, reaffirmed in its order denying the protester's Motion for Rehearing and Leave to Adduce Additional Evidence, that the questions presented were essentially legal, *see infra* at 10 nn. 9 & 10, and 11 n. 11, we believe that the principle stated must be considered as a substantive rule of law rather than a presumption. The Commission recognized at oral argument that the burden of finding the merger

the issuance of the exemptive order. It was the basis of the Commission's denial of the protester's Petition for Rehearing and Leave to Adduce Additional Evidence [9] as well as the argument stressed by the General Counsel for the Commission in its brief [10] and at oral argument.[11] The departure from net asset value re-

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terms reasonable and fair is on it, not the protesters who have neither the financial nor technical means to challenge the evidence of the companies. This recognition was essential in light of the language of the statute. For a general discussion on the legal effects of a presumption, *see* 2 Davis, ADMINISTRATIVE LAW TREATISE § 15.04 (1958); IX WIGMORE ON EVIDENCE §§ 2490-2492 (1940).

[9] The Commission said at n. 5:

> In footnote 38 to our opinion (Release at p. 14, 5 SEC Docket at 754) we said that "The questions presented are in our view essentially legal."

Christiana Securities Company, Investment Company Act Release No. 8692 (February 27, 1975).

[10] It said:

> Realistically, Christiana must be viewed as being substantially equivalent to its Du Pont holdings, and any substantial departure from the value of that stock as a basis for valuing Christiana would ignore the economic realities.

[11] Counsel for the Commission said:

> In economic realities what is being done here is there is being traded one share of Du Pont stock for one share of Du Pont stock, except there is a 2.5% discount, or advantage, given to the Du Pont people because they have to go and vote this thing through and agree with it. And basically this is the fundamental economic test that the Commission believes in its operation of the Act that Congress intended should be followed and that it has followed in past cases.
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> * * * *
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> The Commission *as a matter of law* feels that to allow anything significantly more than two and one-half percent discount would not be fair and that's the reason why the Commission said it isn't material to us that these negotiations were [not] conducted really at arm's length. * * * It is our responsibility to determine whether it is fair. And in determining whether it is fair the Commission feels firmly that the legal test is, is are each side getting the net value * * *. (Emphasis added.)

flected in the two and five-tenths percent (2.5%) discount was accepted only because of the "striking disparity between the substantial benefits to be received by Christiana and the far more modest ones inuring to Du Pont", and because it did not "divest Christiana's stockholders of a significant portion of the intrinsic investment values to which they are legally and equitably entitled." *Christiana Securities Company, supra* at 25-26.

A. The plain language of the Act does not permit the Commission to establish a rule of law that closed-end, non-diversified companies should be presumptively worth the value of their net assets.[13] The Act was drafted with a good deal of specificity. In effectuating its remedial purposes, we will not give it a construction that strains its plain meaning. *See Willheim v. Murchison,* 342 F.2d 33, 42 (2nd Cir.), *cert. denied,* 382 U.S. 840 (1965). Section 17(b)(1) provides:

> The Commission shall grant such application and issue such order of exemption *if evidence establishes* that—
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> (1) the terms of the proposed transaction, including the consideration to be paid or received, *are* reasonable and fair and do not involve overreaching

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[13] Covington & Burling, counsel for Du Pont, advised each financial adviser before their evaluations were made as follows:

> In general, the Commission examines proposed transactions in the light of all relevant financial considerations. In passing on merger terms affecting common stock, the Commission has looked to such factors as comparative earnings, dividends, market values and net asset values (including adjustments for potential taxes arising from unrealized capital gains in portfolio securities and the tax benefits resulting from tax loss carry-forwards). No single factor has been considered determinative.

on the part of any person concerned; * * *
(Emphasis added.)

We read the section to require the Commission to find affirmatively that the terms of each merger are reasonably and fair, a requirement that must be fulfilled even though there are no protesters to the merger.[13] As was said in *Grace v. Ludwig,* 484 F.2d 1262, 1268 (2nd Cir. 1973), *cert. denied,* 416 U.S. 905 (1974):

> The statute here did not envisage a simple reporting procedure or the mere submission of written materials for pro forma or perfunctory review. * * * The Commission could only issue such an order if *evidence* establishes that the consideration to be paid was reasonable and fair and did not involve overreaching * * *.
> (Emphasis included.)

The section does not limit the considerations relevant to the approval of a merger to the preservation of the net asset value of the investment company.

The Commission argues, however, that this result

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[13] The Commission takes the position that its duty to insure fairness under § 17(b)(1) extends to the shareholders of the affiliated company as well as those of the investment company. *Fifth Avenue Coach Lines, Inc., et al.,* 43 S.E.C. 635, 639 (1967). We agree. This is consistent with the purposes of the Act, for, as stated in § 1(a)(3), investment companies may dominate and control the policies and management of companies engaged in interstate commerce. As was said in an analogous context:

> [A] plan of reorganization which is unfair to some persons may not be approved by the court even though the vast majority of creditors have approved it.

TMT Trailer Ferry v. Anderson, 390 U.S. 414, 435 (1968) (footnote omitted) (corporate reorganization under Chapter X of the Bankruptcy Act, 11 U.S.C. § 501 *et seq.*).

obtains when §17(b)(1) is read in conjunction with §2(a)(41)(B). The latter section states:

> "Value", with respect to assets of registered investment companies * * * means—
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> * * * *
>
> (B) * * * with respect to securities for which market quotations are readily available, the market value of such securities; * * *
>
> Nothwithstanding the fact that market quotations for securities issued by controlled companies are available, the board of directors may in good faith determine the value of such securities: *Provided,* That the value so determined * * * is not in excess of market value in the case of other controlled companies.

But §2(a)(41)(B) is not by itself operative, for it neither proscribes nor requires particular conduct. It is only definitional, giving meaning to the term "value" when used in the operative sections of the Act. *See, e.g.,* §§ 3(a)(3), 10(d)(4) and 18. It is not made operative by §17(b)(1) which speaks in terms of "fairness" and not "value." Had Congress intended the construction advanced here by the Commission, there would have been no need to require the Commission to find merger proposals reasonable and fair on the basis of the evidence presented. Congress could have simply decreed that a merger of a closed-end, non-diversified investment company into its portfolio affiliate is reasonable and fair when the investment company is valued at or close to its net asset value. Congress did not do so. Further, §2(a)(41)(B) defines the value of an investment company's assets and not

its stock. In this readjustment of the ownership of Du Pont stock, we look to the value of what the Christiana shareholders are giving in the exchange, considering the net asset value of the company as one relevant factor.

The Commission's reliance on §23(b) to support its position is also misplaced. That section states in its relevant part:

> No registered closed-end company shall sell any common stock of which it is the issuer at a price below the current net asset value of such stock * * * except (1) in connection with an offering to the holders of one or more classes of its capital stock; (2) with the consent of a majority of its common stockholders; (3) upon conversion of a convertible security in accordance with its terms; * * * (5) under such other circumstances as the Commission may permit by rules and regulations or orders for the protection of investors.

Again, the statute does not by its terms apply to the transaction here, for Christiana is not selling any stock of which it is the issuer. The harm intended to be remedied by the statute was the issuance of investment company common stock to favored persons at less than true value resulting in the dilution of the ownership equity of the existing shareholders. *See* Jaretzki, *The Investment Company Act of 1940,* 26 Wash. U. L. Q. 303, 328 (1941). That harm is not present here. The Supreme Court addressed itself to this point recently:

> In deciding whether borderline transactions are within the reach of the statute, the courts have come to inquire whether the transaction may serve as a

vehicle for the evil which Congress sought to prevent * * * thereby endeavoring to implement congressional objectives without extending the reach of the statute beyond its intended limits. * * * Under these strict terms, the prevailing view is to apply the statute only when its application would serve its goals.

Kern County L. Co. v. Occidental Petroleum, 411 U.S. 582, 594-595 (1973). *Accord, Willheim v. Murchison, supra* at 42.

The Commission's discussion of §23(b) treats Christiana as an open-end investment company. Christiana is a closed-end company and, unlike its counterpart, its shareholders have no statutorily protected means to redeem their stock and receive their proportionate share of the company's net assets. *Cf.* 15 U.S.C. §80a-22(e); *U. S. v. National Assn. Securities Dealers*, 45 L.Ed.2d 486 (1975). Unlike the stock of an open-end company, the stock of Christiana actively trades in a secondary market that has historically imposed upon sellers a discount from net asset value. This discount is an economic fact affecting the value of its stock and cannot be ignored in determining what is reasonable and fair.

In economic fact, the shareholders of Christiana do not own the assets of their company. They, like the shareholders of any corporation, own only a pro rata share of the assets and the income derived therefrom.[14]

[14] Charles C. Townsend, Jr., a partner of Morgan Stanley & Co., and managing director of Morgan Stanley & Co., Inc., an affiliated corporation testified:

Q. They [the shareholders of Christiana] would sacrifice the principle of diversification because of the fact that they were holding du Pont shares underpriced; is that correct?

See Jaretzki, *The Investment Company Act of 1940, supra* at 304-305. It is the current worth of the Christiana stock given in exchange for the Du Pont stock that must be determined in order to pass on the reasonableness and fairness of the merger.

B. The legislative history of the Act is consistent with the view that the Commission must look to the value given and received by the respective shareholders to a merger and may not conclusively presume that mergers based on the net asset value of a closed-end, non-diversified investment company are reasonable and fair. That history envisions that the Commission's rulings under §17(b)(1) will be preceded by an inquiry into the relevant facts that is both thorough and independent.

Speaking to the effects of the absorption of one company's assets into another, whether by merger, consolidation or sale of assets, the Commission said:

> The ultimate result of all of these procedures is the concentration of the assets of one or more formerly independent companies in one of the old companies or in a new company. Securities of the successor company are issued for the securities of the old companies. In the achievement of this result, a nonjudicial reorganization of the rights, privileges, and financial position *of the stockholders* of the various companies is accomplished.

A. No, no. I haven't said they were underpriced. They sold for what they were, the assets and earnings and dividend and so on that Christiana had, and sold on that basis as a separate stock in the market.

Townsend's observations paralleled those of Mr. Justice Holmes in *Galveston, H. & S.A.R. Co. v. Texas,* 210 U.S. 217, 226 (1908):

> [T]he commercial value of property consists in the expectation of income from it * * *.

SEC, REPORT ON THE STUDY OF INVESTMENT TRUSTS AND INVESTMENT COMPANIES: ABUSES AND DEFICIENCIES IN THE ORGANIZATION AND OPERATION OF INVESTMENT TRUSTS AND INVESTMENT COMPANIES, H.R. Doc. 279, 76th Cong., 1st Sess. (1939-1940) at 1411 (emphasis added).

And in identifying the evils to be remedied, the report continued:

> [T]hese voluntary plans of readjustment of the rights and values of the holders of shares of corporations, which may involve a change in the character of a stockholder's investment at least as drastic in nature as that accomplished by a judicial reorganization, are not subjected to the scrutiny of any unbiased authority. In judicial reorganizations, the fairness of the plan is a subject of judicial inquiry. * * *
>
> Investment company officials advocated similar safeguards with respect to plans of merger, consolidation, sales of assets or exchange offers.

Id. at 1427-1428.

Subjecting proposed plans of merger to the scrutiny of independent review was found necessary because the presumption of the state statutes that "* * * the directors of the several corporations involved in negotiations for a merger * * * ***are acting at arm's length in an endeavor to secure the best possible bargain for their respective stockholders***" was untrue in practice. *Id.* at 1414 (emphasis added). The Commission made other relevant comments:

> Where * * * several corporations are under common control * * * the possibility of a * * * merger

* * * which is disadvantageous to minority stockholders becomes apparent. * * * Minority stockholders are without unbiased representatives to negotiate the terms of * * * merger agreements. In this situation the intent and spirit of the state merger * * * statutes may be substantially nullified.

Id. at 1414.

[T]he remedy by appraisal is an inadequate one. The statutes do not require that stockholders be informed of their right of appraisal. * * * Even if stockholders are cognizant of their right to an appraisal, the procedure prescribed by the statutes for obtaining it is highly technical and costly. * * * "It is a remedy which does not prevent or set aside inequitable corporate readjustments. * * *."

Id. at 1422 (footnote omitted).

[J]udicial proceedings * * * [are] expensive and usually beyond the means of the average investor * * *. And stockholders who actually sue, although they do so technically in behalf of themselves and all other stockholders, usually are interested in their own welfare only. As a consequence, the actions of suing stockholders in many instances may be settled by managements who fear that a case for equitable relief is clear or probable.

Id. at 1423.

Thus, the Act requires prohibited transactions to be shown in advance of their execution to be reasonable and fair and not the product of overreaching by any person. *See Securities & Exch. Com'n v. Advance Growth Capital Corp.,* 470 F.2d 40, 42-43 (7th Cir. 1972). The thrust of the section, as evidenced by its

legislative history, is that the Commission must require merger proposals to be within the range that arm's-length bargainers would agree to if they were negotiating the terms of the merger.

The Commission states that the absence of arm's-length bargaining "matters not." We disagree. We do, however, agree with the Commission that, because of the relationship of the parties, the Act places its primary concern on the fairness of the results of the negotiating process. But "fairness" is a relative term; and in judging transacting between dominant and subserviant parties, the test is "whether or not under all the circumstances the transaction carries the earmarks of an arm's length bargain." *Pepper v. Litton*, 308 U.S. 295, 306-307 (1939) (footnote omitted).[15] It is only scrutiny of this character that will provide the protections under the Act intended by Congress and it is this that the Commission failed to do here.[16]

C. The Commission's prior decisions lend little support to its holding that Christiana should be valued exclusively on the basis of its net assets. No cases,

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[15] *Pepper v. Litton*, 308 U.S. 295 (1939), was concerned specifically with the power of the bankruptcy court to disallow a judgment obtained by the dominant and controlling shareholder of a bankrupt corporation. But the proposition cited is one of general application to corporate law and equity. *See Consolidated Rock Products Co. v. Du Bois*, 312 U.S. 510, 522 (1941); *Southern Pacific Co. v. Bogert*, 250 U.S. 483, 487-488 (1919). It characterizes the type of unbiased scrutiny found in judicial reorganizations which Congress intended to embody in the Act and to require of the Commission.

[16] The Commission has the statutory power to go beyond the evidence presented by the applicants and compel additional testimony, if necessary, for the proper determination of the issue. *See* 15 U.S.C. § 80a-41.

either cited to us or found by our independent research, holds that method of valuation proper as a matter of law. To the contrary, in those cases where the applicants or the Commission has stated that the respective net asset values of the merging corporations were the principal basis for the merger exchange ratio, other factors relevant to the issue of reasonableness and fairness were considered: *Townsend Corporation of America,* Investment Company Act Release No. 4045 (September 2, 1964) (earnings); *Harbor Plywood Corporation, et al.,* 40 S.E.C. 1002 (1962) (liquidation value, market price and dividends); *Century Investors, Inc., et al.,* 40 S.E.C. 319 (1960) (earnings and dividends); *New York Dock Company et al.,* 38 S.E.C. 754 (1958) (dividends and market value); *International Mining Corporation, et al.,* 37 S.E.C. 209 (1956) (market price); *Central States Electric Corporation,* 30 S.E.C. 680 (1949) (capital gains taxes on the unrealized appreciation of assets).[17]

Other cases cited to us and relied upon by Christiana and Du Pont for the stated rule of law are perfunctory approvals of applicants' proposals decided without contest or hearing. *See Huyler's,* Investment Company Act Release Nos. 5773, 5809 (August 13 and September 9, 1969); *Eastern States Corporation,* In-

[17] The Commission, pursuant to Chapter X of the Bankruptcy Act, issued an advisory report on the reorganization of Central States and considered net asset value. But that value was adjusted to reflect the capital gains taxes on the unrealized appreciation of the assets. The adjustment was necessary to determine the current worth of each shareholder's interest and the extent of their continued participation because the company was reorganized as an open-end investment company required to continually redeem its stock.

vestment Company Act Release Nos. 5693, 5711 (May 28 and June 16, 1969); *Southport Commercial Corporation,* Investment Company Act Release Nos. 4165, 4180 (February 17 and March 5, 1965); *Detroit and Cleveland Navigation Company,* Investment Company Release Nos. 3082, 3099 (July 27 and August 19, 1960). As such, they can be given little weight in determining whether the stated and relied upon rule of law is a valid one. *See Securities and Exchange Com'n v. Sterling Precision Corp.,* 393 F.2d 214, 220 (2nd Cir. 1968).

Applicants cite *Delaware Realty and Investment Company et al.,* 40 S.E.C. 469 (1961), as supportive of the Commission's decision. There, the Commission approved, without hearing, the merger of Delaware Realty, also a closed-end, non-diversified investment company, into Christiana. In doing so, it gave the greatest weight to the net asset values of the merging corporations. It reasoned:

> In view of possible alternatives to a merger, under which the shareholders of Delaware and Christiana could realize the net asset value or underlying net asset value of their shares through an exchange for underlying assets or liquidation, greatest weight was given in the plan of merger to the relative net asset or underlying net asset values of the shares of the two companies. Since such alternatives to a merger would, however, impose tax liabilities upon shareholders and involve other problems, it was determined that statutory meger would be in the best interests of shareholders. No adjustment was made net asset values for capital gains taxes which

> would be payable upon a sale of assets, since the alternatives to merger would not result in taxes to the constituent companies, and the proportion of unrealized appreciation to net asset value is, in any event, substantially the same in the case of both companies.

Id. at 473.

This record does not show that other viable alternatives are available for Christiana to realize its net asset value. *See infra* at 36.

Also cited are *Christiana Securities Company*, Investment Act Release No. 4876 (March 15, 1967) and *Christiana Securities Company*, Investment Company Act Release No. 4155 (January 28, 1965), where the Commission approved an exchange of Christiana common stock for the stock of Hercules Incorporated and General Motors Corporation, respectively. They are perfunctory approvals, granted without a statement of reasons, and are, therefore, entitled to little weight.

In other cases, not cited to us by the applicants or the Commission, proposed merger terms based principally on the respective market values, with consideration also given to dividends, earnings and net asset value, have been found to be reasonable and fair.

Electric Bond and Share Company, Investment Company Act Release No. 5215 (December 28, 1967), was decided after public hearing in which protesters argued that the terms were unfair to both companies. The terms provided for the merger of American & Foreign Power Company, Inc., into Electric Bond and Share. We quote the Commission's conclusion:

> We have considered the various factors relevant

to the fairness of the merger terms. Initially, we note that the shareholders of both companies will derive certain benefits from the amalgamation of the companies. * * *

We have found that the market's evaluation of the stock of the two companies presests a guide to the value of the companies, and that on the basis of the market price relationship, * * * the proposed exchange ratio would provide Foreign Power's shareholders with a premium over the market price ratio. On the other hand, the initial post-merger dividend will represent a far greater dividend increase for the shareholders of Bond and Share than for the Foreign Power shareholders. Relative net asset values at face amount point toward a higher exchange ratio than that proposed; however, as we have found, Foreign Power's assets cannot be accepted at their face amount. We also note that on the basis of 1966 consolidated earnings, the exchange ratio would be favorable to Bond and Share's stockholders, but if consideration is given to realized capital gains the exchange ratio would be favorable to Foreign Power's shareholders.

Id. at 20.

The Commission's aproach to the issue of the reasonableness and fairness of the merger is strikingly different from that espoused here. Economic and not legal considerations were found dispositive. *See also Southeastern Capital Corporation,* Investment Company Act Release Nos. 4110, 4133 (December 23, 1964 and January 12, 1965) (merger based on the market and asset values of the respective companies approved by the Commission without hearing).

We further note that in *Tally Industries, Inc.*, Investment Company Act Release No. 5953 (January 9, 1970), the Commission declined to grant an exemption order under §17(b)(1), finding the *pro forma* after merger earnings and dividends to be inadequate to one of the constituent companies. Again, factors other than net asset value were found determinative.

The Commission's method of valuing investment companies has not been consistent, perhaps reflecting the fact that each case turns upon its particular facts. *See generally* C. Bosland, VALUATION THEORIES AND DECISIONS OF THE SECURITIES AND EXCHANGE COMMISSION (1964). Thus, we are not here confronted with a consistent interpretation of the Act by the agency charged with its enforcement meriting deference by a reviewing court. *See U. S. v. National Assn. Securities Dealers, supra* at 504; *County of Marin v. United States,* 356 U.S. 412, 420 (1958). Moreover, we are unaware of any decision of the Commission that applied the stated rule of law which was subsequently approved by a reviewing court.[18]

It, thus, appears that the Commission's argument that valuation is a legal question is not only new to this

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[18] In *Joan M. Harriman, et al v. E. I. DuPont de Nemours and Company, etc.*, Civil Action No. 4721 (December 23, 1975), the United States District Court for the District of Delaware considered, *inter alia*, whether the proposed merger of Christiana into Du Pont was violative of Rule 10b-5, 17 C.F.R. § 240. The District Court held that it was not. It indicated in dicta that it accepted the Commission's view that net asset value is the fundamenal valuation criterion of registered investment companies. It did so without a detailed examination of the precedents cited by the Commission. We disagree with the dicta but express no opinion on the Rule 10b-5 issue.

case, but is unsupported by its own precedent or that of a reviewing court.

D. The practice under similar statutory standards developed in the judicial supervision of corporate reorganizations also militates against acceptance of the Commission's position.

In construing the "just and reasonable" standard under the Transportation Act of 1940, 49 U.S.C. §1 *et seq.*, the Supreme Court said:

> [T]he merger terms, as to stockholders, must be found to be just and reasonable. These terms would be largely meaningless to the stockholders if their interests were ultimately to be settled by reference to provisions of corporate charters and of state laws. * * * Public regulation is not obliged and we cannot lightly assume it is intended to restore values, even if promised by charter terms, if they have already been lost through the operation of economic forces. * * * In appraising a stockholder's position in a merger as to justice and reasonableness, it is not the promise that a charter made to him but the current worth of that promise that governs, it is not what he once put into a constituent company but what value he is contributing to the merger that is to be made good.[19]

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[19] The Court further said:

> In determining whether each class of stockholders received an equivalent of what it turns in, the Commission, of course, is under a duty to see that minority interests are protected, especially where there is an absence of arm's length bargaining or the terms of the merger have been imposed by management interests adverse to any class of stockholders.

Schwabacher v. United States, 334 U.S. 182, 201 (1948).

Schwabacher v. United States, 334 U.S. 182, 198-199 (1948) (citations omitted). *Accord, Securities and Exch. Com. v. Central-Ill. Sec. Corp.,* 338 U.S. 96, 129 (1949) (review under the "fair and equitable" standard of the Public Utility Holding Company Act, 15 U.S.C. §79k(e)). We believe the inquiry under the Act must be similar. The desires of Christiana shareholders to realize the net asset value of their company, not protected by statute or contract, are not determinative. The reasonable and fair standard of the Act requires that economic and not legal doctrine guide the Commission's inquiry. *See Schwabacher v. United States, supra* at 200; *Moulded Products, Inc. v. Barry,* 474 F.2d 220, 225-226 (8th Cir.), *cert. denied,* 412 U.S. 940 (1973); *Nanfito v. Tekseed Hybrid Co.,* 473 F.2d 537, 541 (8th Cir. 1973). The inquiry must be both independent and thorough, giving consideration to all factors affecting the value of what the Christiana shareholders are contributing to the merger.[20] *See TMT Trailer Ferry v. Anderson,* 390 U.S. 414, 442 (1968); *Securities and Exch. Com. v. Central-Ill. Sec. Corp., supra* at 144-145; *Schwabacher v. United States, supra* at 201; *Consolidated Rock Products Co. v. Du Bois,* 312 U.S. 510, 526 (1941); *Case v. Los Angeles Lumber Products Co.,* 308 U.S. 106, 115 (1939).

The rule in tax law is also contrary to the Commis-

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[20] One scholar notes:

> Current investment value theory seems to have turned away from book or asset value and has placed almost exclusive emphasis upon future returns expected from a stock, whether they take the form of earnings, dividends, capital appreciation, or ultimate sale price or liquidation payment.

Banks, "A Selective Inquiry Into Judicial Stock Valuation," 6 Ind. L. Rev. 19, 38 (1972) (footnote omitted).

sion's view that the issue of proper valuation can be determined on legal, and not economic, principles.

[T]he general principle of the Treasury Regulations is that the value of property is to be determined by its fair market value at the time of the decedent's death. "The fair market value is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts." Treas Reg § 20.2031-1(b). The willing buyer—willing seller test of fair market value is nearly as old as the federal income, estate, and gift taxes themselves * * *. *United States v. Cartwright,* 411 U.S. 546, 550-551 (1973). *See also Hamm v. C.I.R.,* 325 F.2d 934, 937 (8th Cir. 1963), *cert. denied,* 377 U.S. 993 (1964); *O'Malley v. Ames,* 197 F.2d 256, 258 (8th Cir. 1952); *Weber v. Rasquin,* 101 F.2d 62, 64 (2nd Cir. 1939). Such a price necessarily accounts for all factors relevant to value.[21]

Paulina Du Pont Dean v. Commissioner, 19 TCM 281 (1960), and *Mary A. B. Du Pont et al., Executors v. Commissioner of Internal Revenue,* 38 U.S. Bd. Tax Appeals 926 (1938), further illustrate this principle.

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[21] [I]t may be said that the present tendency of the courts seems to be to give consideration to all elements, giving more or less weight to individual factors as the circumstances of the case may require, but without pinpointing any one as being finally determinative. It appears, however, that absent special circumstances, the courts will give first importance to earning power as a valuation factor.

Körner, "Issues and Problems in Valuing Closely Held Business Interests for Estate Tax Purposes, Especially Partnership Interests," N.Y. Univ. 30th Annual Inst. on Fed. Tax., 185, 193 (1972) (footnotes omitted).

In *Paulina Du Pont Dean,* the issue presented was the value of four thousand (4,000) shares of Nemours Corporation for gift tax purposes. Nemours owned stock in Delaware Realty and Investment Company which owned stock in Christiana, Du Pont and Hercules Powder Co. Christiana owned stock in Du Pont, General Motors Corporation, Wilmington Trust Company and the News-Journal Company. The court valued Christiana at 79.42% of net asset value, Delaware Realty at eighty-six percent (86%) of its net asset value and Nemours at eighty percent (80%) of its net asset value, for a cumulative discount of fifty-four and six-tenths percent (54.6%) discount. The discounted value of Delaware Realty and Nemours reflected primarily the consideration given to their earnings, dividends and taxes. In valuing Christiana, the court stated:

> [W]e can discern no reason for using any figure as the value of Christiana * * * other than the market or the bid and asked prices * * *. The mean between the bid and asked prices of Christiana common reflects a 20.58% discount from the net asset value of that security and it is considered unrealistic to assume a liquidation by sale of the assets.

Id. at 287.

In *Mary A. B. Du Pont,* the issue was the value of Christiana and Delaware Realty common stock for estate tax purposes. Christiana was found to have a net asset value per share of $1,760.60 and Delaware Realty a net asset value per share of $15,043.66. But after considering other factors relevant to value, *e.g.,* the taxes incurred should the companies sell their as-

sets for diversification or some other purpose, the investor's primary reliance on dividend payout, and the lack of market for Christiana stock, the court found the value of the stock to be one thousand dollars ($1,000) per share and eight thousand five hundred dollars ($8,500) per share, respectively. In the case of Christiana, this represented a forthy-three and two-tenths percent (43.2%) discount.

The Delaware law of statutory appraisal further exemplifies the error of the Commission's holding. In valuing the stock of a closed-end investment company, the Delaware Court of Chancery said:

> The basic concept of value under the appraisal statute is that the stockholder is entitled to be paid for that which has been taken from him, viz., his proportionate interest in a going concern.
>
> * * * *
>
> The important thing to bear in mind is that value of stock in a going concern is to be measured in terms of ability to realize that value through various media.

Tri-Continental Corporation v. Battye, 31 Del. Ch. 523, 74 A.2d 71, 72, 76 (1950). Du Pont's counsel, commenting on this case, noted that "the decision quite clearly indicates that net asset value is not determinative of value in proceedings under the Delaware appraisal statute, market discount is of great, if not controlling, importance." We agree with the observation. The requirement of the Act that merger terms be reasonable and fair is, of course, not determined by the appraisal laws of the states. But, these laws are rele-

vant in considering the worth of the Christiana shareholders' investment in their company.

To summarize, we hold that the Commission erred in deciding, as a matter of law, that Christiana should be valued on the basis of its net assets (primarily stock in Du Pont).[22] We reach this conclusion from the language of the Act, the legislative history of the Act, a study of the relevant decisions of the Commission, and an examination of related areas of the law.[23]

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[22] The Commission similarly erred in holding that the terms of the merger were reasonable and fair because no detriment was incurred by Du Pont or its shareholders. Lack of detriment is, like net asset value, just one factor to be considered in determining the reasonableness and fairness of a merger.

[23] The United States District Court in ***Joan M. Harriman, et al v. E. I. DuPont de Nemours and Company, etc.***, Civil Action No. 4721 (D. Del., December 23, 1975), found the instant merger fair under Delaware law. It cited in support of its holding ***David J. Greene & Co. v. Dunhill International, Inc.***, 249 A.2d 427 (Del. Ch. 1968); ***David J. Greene & Co. v. Schenley Industries, Inc.***, 281 A.2d 30 (Del. Ch. 1971); ***Meyerson v. El Paso Natural Gas Company***, 246 A.2d 789 (Del. Ch. 1967); and ***Getty Oil Company v. Skelly Oil Company***, 267 A.2d 883 (Del. 1970). We note that the first case cited imposed a standard of intrinsic fairness in determining whether to approve a merger between a dominant and subserviant corporation, but that the last three cases cited required a lesser showing of fraud or palpable overreaching as a condition to setting aside the corporate transactions involved. We acknowledge and give weight to the District Court's decision on Delaware law. We will not state whether we believe it was properly applied. We simply hold that the federal test of reasonableness and fairness has not been met here.

III. THE RECORD AS A WHOLE DOES NOT SUPPORT THE COMMISSION'S GENERAL FINDING THAT THE TERMS OF THE MERGER ARE REASONABLE AND FAIR.

There remains the question whether the Commission's general finding of reasonableness and fairness can be sustained on the record as a whole.[24] The applicants urge that it can. They reason: (A) that because the merger proceedings were carefully structured to provide as nearly as possible for arm's-length bargaining, we should give substantial weight to the bargain reached; and (b) that when all factors are considered, the record supports the Commission's general finding that the terms of the merger are reasonable and fair.[25]

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[24] We might ignore the question on the theory that the Commission had not clearly focused on it because of its erroneous views of the law. We reject that alternative because: the applicants offered extensive oral and written testimony with respect to the issue and do not argue that the record is incomplete; the Commission discussed much of the evidence relating to the question; there have already been extensive delays in the administrative process; and the applicants urge the correctness of the general finding.

[25] We review the Commission's decision in the light of Judge Harold Leventhal's statement in *Greater Boston Television Corporation v. FCC,* 444 F.2d 841 (D.C. Cir.), *cert. denied,* 403 U.S. 923 (1971):

> A court does not depart from its proper function when it undertakes a study of the record, hopefully perceptive, even as to the evidence on technical and specialized matters, for this enables the court to penetrate to the underlying decisions of the agency, to satisfy itself that the agency has exercised a reasoned discretion, with reasons that do not deviate from or ignore the ascertainable legislative intent. "The deference owned to an expert

A. We cannot give substantial weight to the bargain reached. Du Pont did take some steps to simulate arm's-length bargaining. It named two directors, C. B. McCoy and Irving Shapiro, who were not shareholders of Christiana or members of the du Pont family to represent it in the negotiations.

McCoy and Shapiro, in turn, retained the First Boston Corporation, an investment banking firm, to advise them on the financial aspects of the merger. First Boston had no previous significant business relationships and no interlocking directors with either Christiana or Du Pont, and neither First Boston nor its officers or directors had any significant stock interest in either Christiana or Du Pont.

The Du Pont negotiators joined with the Christiana negotiators in retaining Morgan Stanley & Co., an investment banking firm, as financial adviser to both companies. Morgan Stanley had previously acted as financial adviser to both Christiana and Du Pont. It had no interlocking directors with either Christiana or Du Pont, and neither the firm nor its partners had any significant stock interest in Christiana or Du Pont.

The Christiana negotiators retained Kidder, Peabody & Co., Incorporated, an investment banking firm, to advise it separately on the financial aspects of the merger. Kidder Peabody had no significant business relationship and no interlocking directorships with either Christiana or Du Pont, and neither the firm nor

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tribunal cannot be allowed to slip into a judicial inertia." Volkswagenwerk Aktiengesellschaft v. FMC, 390 U.S. 261, 272, 88 S.Ct. 929, 935-936, 19 L.Ed.2d 1090 (1968).

Id. at 850 (footnote omitted).

its officers or directors had any significant stock interest with either Christiana or Du Pont.

The steps taken with respect to the composition of the negotiating committee were inadequate.[26] McCoy and Shapiro were full-time employees of the corporation; they were selected for the negotiating committee by a Board of Directors presumptively controlled by Christiana; they had their compensation fixed by a six-man Bonus and Salary Committee, three of whom owned stock in Christiana;[27] and McCoy was a trustee of the Wilmington Trust Company which holds fifty-six percent (56%) of Christiana's stock in trust and votes sixteen percent (16%) of that stock without consultation with beneficiaries.

We do not suggest that it was improper for the Board of Directors of Du Pont to choose McCoy and Shapiro to serve on the negotiating committee. Their knowledge and expertise were undoubtedly important. We only suggest that the arm's-length nature of the bargaining would have been strengthened had the Du

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[26] The presence of independent boards of directors and independent financial advisers is a relevant factor in determining whether proposed merger terms are reasonable and fair. *See LaSalle Street Capital Corporation,* Investment Company Act Release No. 6693 (August 23, 1971) at 7; *Tally Industries, Inc.,* Investment Company Act Release No. 5953 (January 9, 1970) at 10.

[27] According to the preliminary proxy statement, the Bonus and Salary Commitee of Du Pont as of the date of the statement included:

Emile F. du Pont;
Hugh R. Sharp, Jr.;
Robert L. Richards;
Robert L. Hershey;
George E. Holbrook;
Howard W. Johnson.

The first three were shareholders of Christiana.

Pont negotiating committee also included highly competent representatives of the non-employee, non-du Pont family shareholders. It would have been further strengthened had the Christiana committee included at least one representative of its non-family shareholders.

We recognize that the recommendations of the negotiating committee were approved by unanimous vote of the Board of Directors of Du Pont, with those Du Pont directors holding Christiana stock not voting. The recusing, while proper, does not change our view with respect to the arm's-length nature of the transaction. All but two of the thirteen directors who voted on the proposed merger, Caryl P. Haskins and Howard W. Johnson, were employees or retired employees of Du Pont. Moreover, it is clear from the record that the Board relied on the recommendations of the negotiating committee when it approved the transaction.

The appointment of financial advisers was also significant, but only limited weight can be given to their recommendations. First, the recommendations were premised in part on the errors of law discussed in Section II of this opinion.

Second, two of the advisers, Morgan Stanley and Kidder Peabody, were, according to the staff of the Division of Investment Management Regulations of the Commission, "influenced by the Applicants to such an extent that the objectivity of their final recommendations was substantially undermined." [28] More-

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[28] The Division stated:

In our view, true independence of financial advisers where fairness is at issue would preclude a situation where the advisers are made aware of their clients' thinking as to proper terms and consciously or not, are likely to tailor their opinions, to some degree, to the results desired. Although it is clear from the

over, according to the same source, the advisers were influenced by each other.[29] The staff's comments are supported by the record as a whole.

Third, the alternatives to merger suggested by Morgan Stanley and Kidder Peabody, as justification for the terms reached here, were not established to be either feasible or realistic.

The applicants initially informed the advisers that a § 333 liquidation of Christiana was a feasible alternative to the proposed merger and that the maximum tax exposure to Christiana shareholders in such a liquidation would be between $40 and $70 million or, at the maximum, a tax liability to Christiana's nontax-exempt shareholders of approximately two and eight-tenths percent (2.8%). In the light of this information, the applicants' financial adviser, Morgan Stanley, told Du Pont that it would not be well advised to push for a discount greater than two percent (2%). Thereafter, Morgan Stanley was advised that a § 333 liquidation was not a feasible alternative because Christiana's tax liability could not be computed with

Record that all the advisers did considerable and highly competent work, how much more credible their final products would have been had they been permitted to hand them over to their clients without the pressures resulting from the knowledge that the negotiators were striving for a 2.5% discount. Obviously, if that had been the case, the recommended ranges could have been sufficiently disparate to require a re-thinking of the merger terms. But, unfortunately, the negotiators sought unanimity so excessively that they diminished substantially the value of the advisers' opinions through the imposition of their own views upon the advisers.

[29] The Commission skirted the objectivity issue by holding that as the issues presented were essentially legal in nature, they could not be resolved by reference to the opinion of financial experts.

any degree of certainty.[30] Notwithstanding this change of circumstances, Morgan Stanley made only a minor adjustment downward of five-tenths of a percent (0.5%) in the discount recommended. An equally minor adjustment was made by Kidder Peabody when it became aware of the same fact. No adjustment was made by First Boston. But this fact is unimportant, for there is no showing that First Boston gave weight to the availability of the alternatives in the first instance. It based its recommendations throughout on the lack of detriment to Du Pont and its shareholders, and its belief that it was not improper for Du Pont to accommodate the Christiana shareholders by an exchange of stock based on the net asset value of Christiana.

Kidder Peabody suggested that Christiasa could improve the market price of its stock by increasing the demand therefor. The suggestion required the initia-

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[30] Tax counsel advised Christiana that "if all the legal questions discussed were resolved against Christiana, the result would be an earnings and profit figure vastly in excess of $85.8 million." It recommended that a § 333 liquidation was not a viable alternative to merger. Mr. L. E. Grimes, Assistant Treasurer of Du Pont, testified that he envisioned a tax as high as $200 to $400 million. A tax liability of that magnitude, via liquidation, would be equivalent to an eight and five-tenths percent (8.5%) to seventeen and two-tenths percent (17.2%) discount from net asset value via merger. It is difficult to understand the Commission's failure to insist that the applicants present more detailed information on the potential tax liability, or have its staff develop the required data. The failure can only be understood as reflecting its legal ruling that protection of the Christiana shareholder's net asset value is the determinative factor in finding the merger reasonable and fair. Under these facts, the Commission's statement that "a liquidation might be much more expensive for Christiana's stockholders than this tax-free plan" can be accorded no weight. *Christiana Securities Company, supra* at 10. It is at best a gross understatement.

tion of a plan whereby electing Christiana shareholders would direct their dividends be paid to a trustee authorized to use the proceeds to purchase Christiana common stock. The trustee would buy in the open market or from the company at net asset value, whichever was lower, and remit the stock to the electing shareholders. Kidder Peabody opined that if shareholders, representing fifty percent (50%) of the stockownership of Christiana, were to accept the plan, the average daily volume of sales of Christiana stock would be doubled and the market discount significantly reduced, if not eliminated, over a period of time. It stated that the technique had been successfully used by the Madison Fund and the Paul Revere Fund. The Commission did not receive testimony in support of the statement, nor did it make an independent analysis of the proposition. Available statistics suggest that the validity of the theory has yet to be demonstrated.[31]

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[31] The accuracy of Kidder Peabody's statement that the technique would be successful is questionable. As reported in Weisenberger Services, Inc., *Investment Companies* (1975) at 52, the year-end discounts for the Madison Fund and the Paul Revere Fund were:

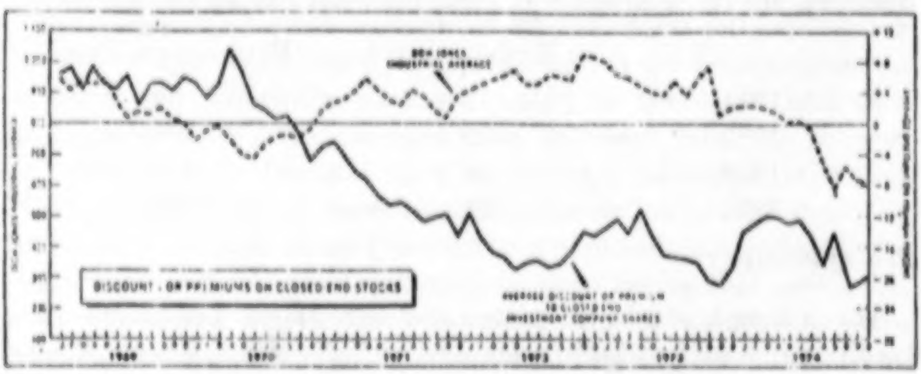
	Madison Fund	Paul Revere Fund
1971	3%	5%
1972	19%	9%
1973	34%	39%
1974	29%	26%

See Appendix I.

The common stocks of closed-end investment companies have traditionally sold at both premiums and discounts from net asset value. The average premium or discount on a sample of closed-end, diversified investment company stocks has varied from a high of about an eight percent (8%) premium in 1970 to a low of about a twenty-two percent (22%) discount in 1974.

Kidder Peabody suggested that another available alternative was for Christiana to solicit a merger partner in the form of an operating company or another investment company. It conceded that the business, financial and legal difficulties were "admittedly large and the time horizon extended" but stated that the alternative must be given some weight. Morgan Stanley, on the other hand, stated that such a merger was unlikely because of the size of the Christiana block and the effect of the United States antitrust laws. On the basis of this record, it has not been shown that merger with another operating company or another investment company is in fact a feasible alternative. The antitrust complications are serious and the size of the block of Christiana severely limits the potential merger partners. At April 28, 1972, market prices, a minimum investment of $860 million would be required to secure control of Christiana.

The applicants belatedly recognized in their application for approval of the merger that the only feasible method for Christiana to achieve its objectives of elimi-



Id. at 22.

nating the intercorporate dividend tax and the potential capital gains tax on the unrealized appreciation of its assets was through a tax-free merger.[82] Unfortunately, by then, the financial advisers' recommendations had already been acted upon.

Fourth, First Boston viewed the transaction simply as an accommodation to existing Christiana shareholders without disadvantage to Du Pont or its shareholders. This view was a candid one and may reflect the most important reason for the Du Pont negotiators agreeing to the terms that they did. The difficulty is that First Boston fails to explain why Du Pont should accommodate Christiana shareholders by paying $491 million more for their stock than it was worth on the open market.

Fifth, the Du Pont negotiating committee initially told the financial advisers that it was receptive to a merger because such action would tend to simplify corporate operations, particularly with respect to actions necessary to comply with the Act, and would broaden the shareholder base. The record indicates that neither factor was a significant one in Du Pont's decision. To the contrary, at hearing, Du Pont's negotiators flatly stated that their objection was to eliminate the Christiana block of stock as a control factor.

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[82] The application states:

From time to time, Christiana has considered various means by which Christiana stockholders could be relieved of the foregoing disadvantages. In view of Federal tax considerations discussed below, the only feasible method available to Christiana to achieve this objective is a tax-free merger into Du Pont. Accordingly, Christiana proposed to Du Pont that such a merger be considered.

We think it demonstrated from the above that the financial advisers acted without a clear understanding of the legal principles involved and that they were neither as independent nor as thorough as they should have been. It follows that the Du Pont Board's unanimous approval of the merger based in part on the financial advisers' report cannot be given substantial weight.

B. The record does not support the Commission's general finding that the terms of the merger are reasonable and fair. The economic benefits to Christiana shareholders from the merger are immediate and substantial. They will receive a premium of twenty-eight and five-tenths percent (28.5%) for their stock ($491,-208,370 on the basis of the April 28, 1972, market price for Christiana); they will share in the undistributed earnings of Du Pont; they will, assuming a payout ratio roughly equivalent to the three lowest of the last five years, receive an increase in dividends of forty-two cents ($0.42) per share (from $5.25 to $5.67); and they will receive a more marketable stock.

The economic benefits to present Du Pont shareholders are minimal. The market value of their shares will be increased by slightly less than four-tenths of one percent (0.4%) ($23 million) as a result of the retirement of approximately 189,000 shares of Du Pont; they will benefit by increased earnings of five cents ($0.05) per share (from $7.31 to $7.36); and they will, assuming a payout ratio as set forth above, receive an increase in dividends of four cents ($0.04) per share ($5.01 to $5.05).

Du Pont negotiators argue that notwithstanding the fact that Christiana shareholders will get the lion's

share of the economic benefits, the merger is nevertheless beneficial for Du Pont and its shareholders. Various reasons, most of which have already been discussed, were advanced for this position at different stages of the proceedings. At the hearing before the Commission, the important benefit to Du Pont was said to be the dispersal of the block of twenty-eight percent (28%) of Du Pont stock held by Christiana. Mr. Irving Shapiro was emphatic in making this point. He stated:

> [T]he central consideration from the du Pont standpoint * * * is the dispersal of a block of 28 percent of du Pont stock in the hands of Christiana. And I say that with a fair amount of diffidence, because, as a matter of history, Christiana has contributed greatly to the success of the du Pont Company over the years. Men such as Pierre S. du Pont, Lamont du Pont, Irenee du Pont, Walter S. Carpenter, Jr., Lamont du Pont Copeland, Crawford H. Greenewalt have all been giants in building the du Pont Company, and they have also been connected with Christiana. * * *
>
> When you look to the future, however, it seems to me we have a totally different picture. And I think this must have underlain the consideration of the Christiana board when Mr. du Pont's letter [suggesting merger] was written.
>
> As these men, some of whom are now gone and others who are now in the latter years of their lives, looked to the future, it strikes me that they must have asked themselves who is going to be managing Christiana in the years to come and what skills do they bring to understanding the chemical industry

and the du Pont Company. And having examined it that way, I suspect they must have concluded it is unwise to deal with uncertainty for the future. But whatever their thinking may have been, from my standpoint the critical consideration for the future of the Du Pont Company—and I am talking about those who follow us in management, rather than the current management—is that there not be a block of 28 percent of du Pont shares in hands of people who have no familiarity with the chemical business and with the du Pont Company in its detailed operations.

And it is the elimination of that kind of an uncertainty for the future which seems to me so overbearing in importance that the merger is the greatest news that I can think of for the du Pont Company.

The Commission viewed the dispersal of control as being more formal than substantive [33] and gave little

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[33] The Commission stated:

The "dispersal" argument is somewhat puzzling. Applicants insist over and over again that it is most unlikely that any substantial number of Du Pont shares will come to market by reason of the proposed transaction. In that regard applicants point quite cogently to the large individual capital gains taxes that selling Christiana holders will have to pay and to the long-run character of the du Pont family's investment commitment to the company that bears its name. What then is likely to be dispersed?

It would seem that the dispersal will be formal, not substantive. Today some people own a great deal of Du Pont indirectly through Christiana. Tomorrow those very same people will still own a great deal of Du Pont. But they will own it directly rather than indirectly. What will that change do for Du Pont?

Du Pont's answers to these questions look to the long run. Its brief concedes that its "management was aware of no immediate prospect of any adverse consequences from the Christiana holdings." The brief goes on to argue, however, "that over the long term such a possibility might arise."

weight to this factor. Its theory was that it could not be concerned with whether Du Pont was controlled by Christiana, the du Pont family, successors to the du Pont family or current management.

We agree with the Commission that the dispersal of control appears to be more formal than substantive. The Wilmington Trust Company would continue to exercise some degree of control over fifty-six percent (56%) of the newly-issued Du Pont stock. The du Pont family would continue to hold more than twenty-two percent (22%) of the Du Pont stock. The Finance Committee[34] and the Bonus and Salary Committee would continue to be controlled by the du Pont family.

The precise nature of these possible long-term adverse consequences is obscure. The argument rests on the possibility of a future clash between the people then in control of Christiana and the people then managing Du Pont. It assumes that in this hypothetical situation the Du Pont managers will be the "good guys" and the Christiana control group the "bad guys." The argument seems far-fetched and rests on premises we consider unacceptable. Christiana's extinction may well make it somewhat easier for Du Pont's managers to maintain themselves in office. We, however, cannot presume that this will necessarily be in the Du Pont stockholders' interest. And in any event the Investment Company Act was not designed to foster the retention of control by managerial groups. Nothing in it warrants a holding that such control is to be preferred to control by important stockholders. (Footnotes omitted.)

Christiana Securities Company, supra at 14-15.

[34] As of the date of the hearing, the Finance Committee consisted of:

Crawford H. Greenewalt (a du Pont family member);
George P. Edmonds (a du Pont family member);
E. F. du Pont (a du Pont family member);
W. S. Carpenter (a du Pont family member);
Edward R. Kane (a Du Pont employee);
George E. Holbrook (a Du Pont employee); and
Charles B. McCoy (a Du Pont employee).

And the family would retain substantial membership on the Board of Directors.

We do not agree with the Commission that dispersal of control is irrelevant in a determination of reasonableness and fairness. Important advantages to Du Pont and the public would flow from an effective dispersion of control. The problem is that the degree of dispersion attained here does not justify the substantial premium paid for the Christiana stock.

Christiana argues that the merger should nonetheless be approved because the economic benefits which its shareholders would receive are largely the result of the operation of the tax laws of the United States, and that they alone are entitled to receive these benefits.[35] We take a different view of the matter. As we see it, Christiana would have us ignore the market value of its stock in determining reasonableness and fairness. We cannot do so. Market value, like net asset value, is a factor which must be considered in determining the worth of an investment. The fact that the marget value

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[35] The Commission stated:

> It might seem that the discount should at the very least equal the 7.2% income tax benefit to be realized by the Christiana stockholders. * * * This consideration, however, we put to one side. The heart of the matter is that the tax benefits to be reaped by the Christiana people will inflict no corresponding detriment on Du Pont or on its stockholders. The burden will fall wholly on the United States. And neither the du Pont family nor the other Christiana holders are under any duty to maximize their tax liabilities.

Christiana Securities Company, supra at 17 n. 44.

We agree that the members of the du Pont family are under no duty to maximize their tax liabilities. Correspondingly, Du Pont is under no duty to the family to assist them in minimizing those liabilities. Fairness requires that Du Pont share in the tax savings that result from its cooperation.

of Christiana stock is affected by the intercorporate dividend tax and unrealized capital gains liabilities is no reason to ignore that value in determining its worth.[36]

We might have a different case if Christiana stock had not consistently sold at a substantial discount from net asset value. The fact is, however, that the discount has not been less than nine and seven-tenths percent (9.7%) and has been as high as thirty and three-tenths percent (30.3%) since April, 1967. The discount has not fallen below seventeen and seven-tenths percent (17.7%) since January 1, 1969.

There perhaps were times in the history of Christiana, particularly before World War II, when the du Pont family could have realized the net asset value of their shares by alternatives other than merger, but they chose to retain the economic, political and social advantages that accompanies control of one of America's largest industrial concerns. Having chosen to do so, they cannot now be heard to complain that the tax laws of the United States have affected the market value of their stock.

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[36] The market value of the stock of most closed-end investment funds is affected by the same factors. *See* B. Malkiel, *A Random Walk Down Wall Street* (1973) (relatively low average returns on assets, unrealized capital gains in fund portfolios, and lack of sales efforts commonly result in discounts from net asset value in closed-end investment funds); K. Boudreaux, *Discounts and Premiums on Closed-End Mutual Funds: A Study in Valuation*, 28 Journal of Finance (May 1973) at 515-522 (discounts and premiums are related to market expectations of the future performance of the fund). The relevance of Boudreaux's conclusion is that this record shows that holders of Christiana stock had no reasonable expectations of greater earnings, or higher prices for their stock unless this merger could be accomplished.

The protesters contend that the consummation of the merger will have a significant adverse market impact on the price of Du Pont stock. The applicants retort that any adverse impact will be minimal and of short duration. They reason that potential capital gains tax liabilities will discourage Christiana shareholders from selling their Du Pont stock, and that the Du Pont market is strong enough to absorb any sales that will be made.[37] The Commission takes still another view:

> We assume that the merger may engender some selling that would otherwise not take place. We assume further that such selling may at certain points

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[37] The federal income tax basis to present holders of Christiana common stock is summarized below:

Basis	*Number of Shares* [a]	*Percent of Total* [a]	*Percent of Subtotal*
\$ 0	2.9mm	25.1	35.7
\$ 0.01-25.00	3.1	26.6	37.8
\$25.01-50.00	0.7	6.4	9.1
\$50.01-100.00	0.8	7.3	10.3
\$100.01-150.00	0.2	2.0	2.8
Over \$150.00	0.4	3.0	4.3
	8.2	70.3	100.0
Held by tax-exempt organizations	1.3	11.0	
No information available	2.2	18.7	
Total shares outstanding	11.7	100.0	

a. Items do not add to totals because of rounding.

The disinclination on the part of the Christiana shareholders to sell their Du Pont stock will be heightened to the extent they are subject to the minimum tax on tax preference income.

in time be substantial. Proceeding on those assumptions, we are nevertheless after considerable thought unable to detect any uncompensated detriment to the Du Pont stockholders of a type that we can properly take into account.

The stock market has its peculiarities. In essentials, however, it is much like other more basic markets in goods, services, and the factors of production. Here as elsewhere increased supply will (all other factors being equal—which in practice they may or may not be) lower prices. Should the Wilmington Trust Company decide to sell a substantial amount of Du Pont common, the price of the issue will be affected to some extent.

We agree with the objectors about that. But we disagree with their contention that this short-run view of the pricing process is the one that governs here. What we have before us in these proceedings is a proposal for a fundamental corporate readjustment. In that context transitory market phenomena are of secondary significance. We look at the case not from the objectors' tape-watcher perspective, but as a problem in economic realities and business fundamentals. (Footnotes omitted.)

Christiana Securities Company, supra at 19-20.

The record supports the view that the merger will engender some selling that would not otherwise take place. The Wilmington Trust Company indicated that it would make sales from time to time, increased marketability generally will result in some additional shares of Du Pont finding their way into the market, and some block selling must be anticipated. It is the

latter sales that may adversely affect the price of Du Pont stock for short periods of time.[38] The Commission would entirely ignore these short-term effects on the grounds that it is not interested in protecting "tape watchers." But persons other than "tape watchers" will be required to sell stock from time to time, and some of them may have to sell their Du Pont stock during a period in which the price of that stock is depressed. Moreover, "tape watchers" deserve the same protection as other investors. It follows that the Commission erred in failing to give any weight to the factor of occasional detriment to Du Pont shareholders.[39]

To summarize: substantial weight cannot be given

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[38] In the first six months of 1972, the median daily volume of Du Pont shares sold was twelve thousand (12,000). Almost one-half of all the daily volumes were between ten thousand (10,000) and twenty thousand (20,000) shares. On three occasions, however, volumes in excess of one hundred thousand (100,000) shares were sold. It thus appears that the market has shown the capacity to occasionally handle large volumes of shares and appears flexible between ten thousand (10,000) and twenty thousand (20,000) shares. The merger agreement, however, provides that once a year an underwritten offering of $25 million in the then current market value of such shares can be made. At the average price of $165.00 in the first six months of 1972, this would approximate 153,000 shares.

[39] The record supports the applicants' contention that the stock of Du Pont will not be significantly depressed for long periods of time. The market for Du Pont is sufficiently broad and strong to absorb not only the large offerings of restricted stock that may be made from time to time, but also to absorb increased daily sales of stock that will flow from the improved marketability of the converted Christiana shares. *See Institutional Investor Study Report of the Securities and Exchange Commission, "Characteristics and Price Impacts of Block Trading in Common Stock Listed on New York Stock Exchange,"* H. R. Doc. 92-64, 92nd Cong., 1st Sess. (1971) at 1537-1828.

to the recommendations of the negotiating committee or the financial advisers; the economic benefits of the merger flow almost entirely to the Christiana shareholders and there are no significant compensating benefits that flow to Du Pont and its shareholders; and the potential detriment to Du Pont shareholders which would result from the merger is minimal but of sufficient import that the Commission should have accorded it some weight in determining reasonableness and fairness.

CONCLUSION

We hold that there is not substantial evidence on the basis of this record to support the Commission's finding that the terms of the merger are reasonable and fair and free from overreaching on the part of anyone concerned. The order of the Commission granting the application to merge is accordingly set aside. Costs will be taxed equally to Du Pont and Christiana.[40]

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[40] The Administrative Office of the United States Courts authorized the appointment of Professor Roger B. Upson, Associate Dean of the University of Minnesota College of Business Administration, to serve as a contract consultant in the office of the Circuit Executive. His duties as a contract consultant were to assist the Court in understanding the record in this case and to prepare reports and memoranda for this Court in connection with that function. Dean Upson's report was filed with the Clerk of this Court and copies thereof were submitted to the parties. The parties have been given an opportunity to respond. Dean Upson's consulting fees were paid by the Administrative Office.

STEPHENSON, Circuit Judge, Dissenting.

I respectfully dissent.

I would affirm the action of the Securities and Exchange Commission in exempting the proposed merger from the proscription of 15 U.S.C. § 80a-17 et seq.[1] I am satisfied that "the Commission's action is based upon substantial evidence and is consistent with the authority granted by Congress." *Securities & Exchange Commission v. Chenery Corp.,* 332 U.S. 194, 207 (1946). *See* 15 U.S.C. § 80a-42(a).

The Commission is granted the broad authority to issue an order of exemption if the evidence establishes that:

> (1) the terms of the proposed transaction, including the consideration to be paid or received, are reasonable and fair and do not involve over-reaching on the part of any person concerned;

15 U.S.C. § 80a-17(b)(1).

The Commission recognized that in applying this test "we must find this transaction fair to the stockholders of both companies. See *Bowser, Inc.,* 43 S.E.C. 277 (1967)." (Comm. Op. at 8 n.22).[2] It took note of the contention of the two companies, Du Pont and Christiana, that in economic reality Christiana stock already is Du Pont stock under another name—98% of Christiana's total assets is Du Pont common stock. Thus the merger involves for all practical purposes

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[1] Section 17(a) of the Investment Company Act of 1940.

[2] The findings and opinion of the Commission reported as *Christiana Securities Company,* Investment Company Act of 1940, Release No. 8615 (December 13, 1974) will be referred to as (Comm. Op.). To avoid repeating matters set out in the majority opinion of this court citation thereto will be as follows: (Slip Op.).

an exchange of equivalents. On the other hand the three objecting Du Pont stockholders contended that the transaction would confer great benefits on Christiana's stockholders; give Du Pont stockholders nothing worth mentioning but actually injure them; and serve no real business purpose for Du Pont. The Commission then proceeded to analyze these contentions.

The benefits to Christiana stockholders [3] will be substantial. They stem from the federal tax structure and stock market phenomena. Under current tax law Christiana pays an effective 7.2% on the dividend income accrued on its Du Pont stock before such dividend is disbursed to Christiana stockholders. The merger eliminates this tax burden. An alternative method of accomplishing the same end could be achieved by liquidation of Christiana but it is conceded that tax consequences would make it more expensive than the merger which is a tax-free plan.[4]

The Commission noted that the tax benefits accruing to the Christiana stockholders

> will inflict no corresponding detriment on Du Pont or on its stockholders. The burden will fall wholly on the United States. * * * Nor do we see how Section 17(b)'s "reasonable and fair" standard can be deemed to require Christiana's stockholders to turn every nickel of their tax savings over to Du Pont.

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[3] Members of the Du Pont family hold about 75% of Christiana, the other 25% belonging to public stockholders.

[4] The merger is designed to be tax-free to Christiana and its stockholders and was conditioned on a ruling to that effect by the Internal Revenue Service. A favorable ruling has now been made. IRS Opinion Letter to Kenneth W. Gemmill, counsel for Christiana Securities Co., December 30, 1975.

> The tax savings are of some weight. But it does not follow that the Du Pont stockholders are to be subrogated to the rights that the United States now enjoys under the status quo.

(Comm. Op. at 17-18 n.44).

Taxpayers, of course, are not prohibited from arranging their affairs so as to minimize taxes. In *Commissioner v. First Security Bank,* 405 U.S. 394, 398-99 n.4 (1972), the Supreme Court observed that

> Taxpayers are, of course, generally free to structure their business affairs as they consider to be in their best interests, including lawful structuring (which may include holding companies) to minimize taxes. Perhaps the classic statement of this principle is Judge Learned Hand's comment in his dissenting opinion in *Commissioner v. Newman,* 159 F.2d 848, 850-851 (CA2 1947):
>
> "Over and over again courts have said that there is nothing sinister in so arranging one's affairs as to keep taxes as low as possible. Everybody does so, rich or poor; and all do right, for nobody owes any public duty to pay more than the law demands: taxes are enforced exactions, not voluntary contributions. To demand more in the name of morals is mere cant."
>
> See *Knetsch v. United States,* 364 U.S. 361, 365 (1960); Chirelstein, Learned Hand's Contribution to the Law of Tax Avoidance, 77 Yale L.J. 440 (1968).

The stock market phenomenon is that Christiana's shares were selling at a discount of 23% when the merger negotiations were first announced and during

the preceding two years the discount had been between 20% and 25%.[5] The objectors and my colleagues insist that the fact that the market value of Christiana stock is affected by the intercorporate dividend tax and unrealized capital gains liabilities is no reason to ignore that value in determining its worth.

The Commission recognized that the benefits to the parties were not equal—the benefits inuring to the Christiana stockholders were greater than to the Du Pont stockholders.[6] Christiana's stockholders could have caused Christiana to be liquidated and thereby achieved the results contemplated by the merger. Admittedly, the merger was designed to avoid serious tax problems that Christiana's liquidation would engender for its stockholders. However, the Commission concluded that these tax-related benefits should not be weighed against Christiana in determining the overall fairness of the merger.

Aside from those tax problems, however, the economic impact of this merger on Du Pont and its

[5] The discount is probably attributable to the intercorporate dividend tax of 7.2% and the fact that Christiana stock is a thinly traded over-the-counter issue whereas Du Pont is an active, well-known listed stock. (Comm. Op. at 22 n.51).

[6] The principal benefits accruing to Du Pont stockholders arise from the merger agreement which provides for the issuance of Du Pont common stock equivalent in value to 97.5% of Christiana's net assets after certain adjustments. The 2.5% discount from Christiana's net asset value amounts to approximately $55 million. It should be noted, however, that since Christiana has a 28.3% interest in Du Pont, 28.3% of the 2.5% discount will go back to Christiana stockholders. Another benefit is the dispersal of control. The Commission accorded this little weight because it viewed the same as being more formal than substantive (Slip Op. at 45-46). I agree with the majority that important advantages to Du Pont and the public would flow from an effective dispersion of control (Slip Op. at 47).

stockholders is no more onerous than the impact that would be produced were the Christiana stockholders to exercise their prerogative to liquidate Christiana. More specifically, the possible market effects resulting from the Christiana stockholders acquiring direct ownership of the Du Pont shares would be the same. It may be that in the course of bargaining between wholly unrelated parties, Du Pont could have exacted a handsome price for permitting consummation of the transaction in a form that relieves the Christiana stockholders of their tax problems. But Du Pont's failure to do that does not render the transaction unreasonable or unfair. The Du Pont stockholders, including the objectors, have no property interest in the Christiana stockholders' tax problems. A principal reason why Section 17 of the Investment Company Act requires us to pass upon the fairness of transactions such as this, is to prevent persons in a strategic position from using that position to effect transactions for other than fair value. And fair value does not change simply because a strategic position arises from something other than affiliation.

(Comm. Op. at 18).

Instead, the Commission viewed the objectors' claim of detriment by reason of market impact to be the crux of the case. Objectors fear that the merger will produce considerable selling of Du Pont that otherwise would not take place and thus the market price would be depressed. Christiana argues there is little reason to believe that the Christiana stockholder will sell the Du Pont shares he receives in the merger because of adverse tax consequences. The tax basis of the Du Pont common stock received by the Christiana com-

mon stockholders who own only Christiana common stock will be the same as the basis of the Christiana common stock surrendered in exchange therefor. My colleagues are of the opinion that "the Commission erred in failing to give any weight to the factor of occasional detriment to Du Pont shareholders." (Slip Op. at 52). I am persuaded that the thrust of the Commission's view is that "[s]peculations about the probable behavior patterns of speculators are much too slender a reed on which to predicate findings of fairness under the Investment Company Act." (Comm. Op. at 22). This disagreement brings into focus the dispute with respect to the valuation standard applied by the Commission in assessing the fairness of the transaction.[7]

It is the Commission's view that:

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[7] Two other items deserve brief comment. The majority is of the view that substantial weight cannot be given to the bargain reached because of the absence of arm's length bargaining (Slip Op. at 34); further that only limited weight can be given the recommendations of the financial advisors (Slip Op. at 36). I do not disagree. Neither does the Commission. The Commission recognized that "[i]t is precisely because transactions of this character are replete with inherent conflicts of interest that the Act requires that they be submitted to us." (Comm. Op. at 26 n.62).

The Commission noted that in some situations the opinions of experts were crucial, e.g., a question about the value of a major league baseball franchise, but such is not the case here. It commented:

> The instant case, on the other hand, involves marketable securities. The questions presented are in our view essentially legal. Hence they cannot be resolved by reference to the opinions of financial experts, however conscientious and however eminent. We do not go so far as to say that expert testimony is of no weight here. Some of it we have found interesting and even instructive. But in view of the nature of the issues raised, we think its weight limited.

(Comm. Op. at 13-14 n.38).

Here justice requires no ventures into the unknown and unknowable. An investment company, whose assets consist entirely or almost entirely of securities the prices of which are determined in active and continuous markets, can normally be presumed to be worth its net asset value. What better guide to its value could there be? The simple, readily usable tool of net asset value does the job much better than an accurate gauge of market impact (were there one) could. The record indicates that most of Christiana's stock is held by long-term investors. Hence there is no pressing need to depart from the net asset value test.[57]

(Comm. Op. at 23-24 & n. 57).

My colleagues insist that the plain language of the

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[57] Investment companies are as a general rule media for long-term investment. That makes net asset value the touchstone. And the Act is based on that premise. Section 2(a)(41)(B) states that "'Value' with respect to assets of registered investment companies . . . means . . . with respect to securities for which market quotations are readily available, the market value of such securities." And although the closed-end discount phenomenon was well-known in 1940, the Congress that passed the Act chose to protect closed-end stockholders against dilution of intrinsic values rather than to facilitate the sale of new closed-end shares. Section 23(b) of the Act shows that. It provides that "No registered closed-end company shall sell any common stock of which it is the issuer at a price below the current net asset value of such stock." And we have viewed net asset value as the controlling factor in Section 17 proceedings. See, e.g., *Harbor Plywood Corporation*, 40 S.E.C. 1002, 1010 (1962); *Delaware Realty and Investment Company*, 40 S.E.C. 469, 473 (1961). Compare *Central States Electric Corporation*, 30 S.E.C. 680, 700 (1949) (advisory report on plans for the reorganization of a closed-end investment company under Chapter X of the Bankruptcy Act urging "net asset value as the primary measure of value of an investment company.")

Act does not permit the Commission to establish as a rule of law that closed-end, nondiversified companies should be presumptively worth the value of their net assets. (Slip Op. at 12, et seq.). I disagree. The Commission in this 17(b) proceeding has been delegated the responsibility of app`,ying the "reasonable and fair" test. Its judgment in applying this broad criterion is not subject to reversal "save where it has plainly abused its discretion." *Securities & Exchange Commission v. Chenery Corp., supra,* 332 U.S. at 208; *accord, Niagara Hudson Power Corp. v. Leventritt,* 340 U.S. 336, 347 (1951); *Securities and Exchange Commission v. Central-Illinois Securities Corp.,* 338 U.S. 96, 126 (1949).[8] The above cases involve application by the Commission of the "fair and equitable" standard of Section 11(e) of the Public Utility Holding Company Act of 1935, 15 U.S.C. § 79k(e). In *Chenery, supra,* 332 U.S. at 209, the Supreme Court spoke as follows:

> The Commission's conclusion here rests squarely in th·⁺ area where administrative judgments are entitled to the greatest amount of weight by appellate courts. It is the product of administrative experience, appreciation of the complexities of the problem, realization of the statutory policies, and responsible treatment of the uncontested facts. It is

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[8] The Congress in numerous statutes has established the Securities and Exchange Commission as the expert government agency in securities matters. Securities Act of 1933, 15 U.S.C. 77a-77aa; Securities Exchange Act of 1934, 15 U.S.C. 78a-78jj; Public Utility Holding Company Act of 1935, 15 U.S.C. 79-79z-6; Trust Indenture Act of 1939, 15 U.S.C. 77aaa-bbb; Investment Company Act of 1940, 15 U.S.C. 80a-1-80a-52; Investment Advisers Act of 1940, 15 U.S.C. 80b1-21.

the type of judgment which administrative agencies are best equipped to make and which justifies the use of the administrative process. See *Republic Aviation Corp. v. Labor Board,* 324 U.S. 793, 800. Whether we agree or disagree with the result reached, it is an allowable judgment which we cannot disturb.

I am persuaded that this language controls our action in this case.

In summary, the proposed merger involves essentially an exchange of equivalents—Du Pont stock for Du Pont stock. The benefits to Christiana stockholders are substantially greater than to Du Pont stockholders. This is due largely to tax consequences. It will be a tax-free exchange. Christiana shareholders avoid the probable tax consequences a liquidation would involve. They also rid themselves of the intercorporate dividend tax of 7.2% which has contributed to the discount in the market value of Christiana shares as compared to Du Pont shares.[9] However, Du Pont shareholders have no property interest in these resultant tax savings. Further, the detriment to present Du Pont common stockholders is dubious. At the most there may be some additional selling of Du Pont stock which will temporarily affect the market value of Du Pont. This is highly speculative. The tax basis of Du Pont stock received by Christiana shareholders in the merger will be the same as the Christiana stock surrendered in exchange therefor. Tax consequences will deter the temptation to sell. Under all the circumstances the Commission concluded that the disparity in bene-

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[9] *See* n.5, *supra.*

fits justified the proposed 2.5% discount ($55 million) from the net asset value of Christiana. It was within the range of fairness. A discount appreciably higher "would divest Christiana stockholders of a significant portion of the intrinsic investment values to which they are legally and equitably entitled" and thus "run afoul of the Act." (Comm. Op. at 26).

The Commission exercising its expertise under applicable statutory authority made a judgment which we cannot disturb.[10] I would affirm.

A true copy.

Attest:

Clerk, U.S. Court of Appeals, Eighth Circuit

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[10] For an additional discussion of the fairness standard under the Act, *see Harriman, et al. v. E. I. Du Pont de Nemours and Co.*, —— F. Supp. ——, Civil No. 4721 (D. Del., December 23, 1975).

APPENDIX

General Information About Investment Companies

Table 5

Year-End Discounts and Premiums

	1974	1973	1972	1971	1970	1969	1968	1967	1966	1965	1964
Diversified Companies											
*Adams Express Co.	25%	14%	14%	15%	6%	P 6%	P10%	6%	6%	12%	10%
Advance Investors	22	21	—	—	—	—	—	—	—	—	—
*Carriers & General	16	19	17	20	18	14	12	21	19	11	6
Consolidated Investment Trust	6	4	4	2	2	4	P 1	1	10	21	14
*General American Investors	13	17	4	12	8	P 8	P14	P 1	11	7	6
*International Holdings Corp.	39	28	27	13	18	10	5	16	25	21	15
*Lehman Corp.	22	20	13	8	P14	P16	P23	P16	9	11	6
*Madison Fund	29	34	19	3	P16	P48	P32	P19	P18	P 2	P 3
*Niagara Share Corp.	P 4	4	7	13	P 5	P12	P 8	11	12	8	0
*Tri-Continental Corp.‡	14	13	19	14	5	2	4	16	25	23	24
*U.S. Foreign Securities	26	21	3	7	3	11	7	17	29	33	26
Diversifitd Investment Company Average	20	19	14	12	3	P 6	P 7	6	13	14	10
Non-Diversified Companies											
Baker, Fentress & Co.	58	54	41	14	—	—	—	—	—	—	—
Central Securities‡	41	40	31	P14	P37	P58	P31	3	P 9	11	P 5
Standard Shares	38	35	25	23	24	13	6	20	21	16	10
United Corporation	25	24	28	26	15	14	7	12	20	24	19
Specialized Companies											
American General Conv. Sec.	3	10	4	—	—	—	—	—	—	—	—
ASA Limited	9	P26	6	P10	P37	15	P54	P77	P12	P 5	10
Bancroft Convertible Fund	22	31	29	14	—	—	—	—	—	—	—
Bayrock Utility Securities	17	24	5	—	—	—	—	—	—	—	—
Castle Convertible Fund	23	29	21	9	—	—	—	—	—	—	—
Chase Convertible Fund	14	19	15	—	—	—	—	—	—	—	—
CNA—Larwin Investment Co.‡	—**	1	—	—	—	—	—	—	—	—	—
Diebold Venture Capital Corp.	69	68	50	51	48	25	7	—	—	—	—
Drexel Utility Shares	5	17	19	—	—	—	—	—	—	—	—
Highland Capital Corp.	67	74	45	47	37	34	—	—	—	—	—
Japan Fund	43	31	8	P 7	P11	P 6	P 5	9	32	27	32
Keystone OTC Fund	39	50	26	—	—	—	—	—	—	—	—
National Avaiation	43	39	27	15	12	15	P26	P38	P14	2	10

New America Fund	58	47	33	58	47	41	0	—	—	—	—
Petroleum Corp.	10	8	4	14	8	P 4	P 7	3	0	P 6	3
Precious Metals Holdings	27	—	—	—	—	—	—	—	—	—	—
REIT Income Fund‡	P34	P10	P 5	—	—	—	—	—	—	—	—
S-G Securities‡	P375	P 2	—	—	—	—	—	—	—	—	—
Source Capital‡	45	49	53	42	33	32	P 3	—	—	—	—
Value Line Development Capital Corp.	70	66	41	49	36	20	P18	—	—	—	—
Bond Funds											
American General Bond Fund	P 1	P 6	P11	P 9	—	—	—	—	—	—	—
Bunker Hill Income Securities	2	10	—	—	—	—	—	—	—	—	—
Circle Income Shares	P 3	P 1	—	—	—	—	—	—	—	—	—
CNA Income Shares	18	8	—	—	—	—	—	—	—	—	—
Current Income Shares	7	15	—	—	—	—	—	—	—	—	—
Drexel Bond-Debenture Trading Fund	13	20	5	P 4	—	—	—	—	—	—	—
Excelsior Income Shares	13	9	—	—	—	—	—	—	—	—	—
Federated Income & Private Placement	8	3	4	—	—	—	—	—	—	—	—
Fort Dearborn Income Securities	5	9	P 5	—	—	—	—	—	—	—	—
John Hancock Income Securities	10	7	—	—	—	—	—	—	—	—	—
John Hancock Investors	12	P 1	P 5	P 6	—	—	—	—	—	—	—
Hatteras Income Securities	1	1	—	—	—	—	—	—	—	—	—
INA Investment Securities	17	19	—	—	—	—	—	—	—	—	—
Independence Square Income Securities	8	P 5	P 3	—	—	—	—	—	—	—	—
Lincoln Nat. Direct Placement Fund	26	23	P 8	—	—	—	—	—	—	—	—
MassMutual Corporate Investors	39	23	2	1	—	—	—	—	—	—	—
MassMutual Income Investors	13	10	P 8	—	—	—	—	—	—	—	—
Montgomery Street Income Inv.	2	12	—	—	—	—	—	—	—	—	—
Mutual of Omaha Interest Shares	12	13	4	—	—	—	—	—	—	—	—
Pacific-American Income Shares	8	14	—	—	—	—	—	—	—	—	—
Paul Revere Investors	26	39	9	5	—	—	—	—	—	—	—
St. Paul Securities	11	15	P 8	—	—	—	—	—	—	—	—
S & P/Intercapital Income Sec.	0	14	—	—	—	—	—	—	—	—	—
State Mutual Securities	11	18	—	—	—	—	—	—	—	—	—
Transamerica Income Shares	17	14	P 6	—	—	—	—	—	—	—	—
USLIFE Income Fund	P 2	11	P 7	—	—	—	—	—	—	—	—
Vestaur Securities	1	0	P 7	—	—	—	—	—	—	—	—

* Companies included in the Diversified Investment Company Average.
** Negative net asset value.
‡ Common Stock.
P Premium.

EFFECTS UPON CHRISTIANA COMMON STOCK OF VARIOUS DISCOUNT VALUES AND DIVIDEND POLICIES.*

MERGER AT SPECIFIED PERCENTAGE OF ADJUSTED NET ASSET VALUE (a)

	100%	97.5%	87.9% (h)	76.9% (i)
Exchange ratio, number of DuPont common for one Christiana (g)	1.152	1.123	1.012	0.884
Earnings per share (b)	$8.42	$8.26	$7.65	$6.91
Percent change from 1971 (c)	+59.5%	+56.4%	+44.9%	+30.9%
Dividends per share, 68.6 percent payout (d,e)	$5.78	$5.67	$5.25	$4.74
Percent change from 1971 (c)	+10.0%	+8.0%	0%	−9.7%
Dividends per share, 74 percent payout (d,e)	$6.23	$6.11	$5.66	$5.12
Percent change from 1971	+18.7%	+16.4%	+7.8%	−2.5%
Premium, April 28, 1972 (f)				
Percent	+31.9%	+28.5%	+15.8%	+1.2%
Total	$548,278,380	$491,208,370	$272,045,010	$20,954,995
Premium, July 17, 1972 (f)				
Percent	+13.1%	+10.3%	−0.6%	−13.2%
Total	$257,634,440	$201,836,500	−$12,442,218	−$257,935,970

* See assumption on following pages, referenced by letters (a) through (i) on this table.

APPENDIX II

EFFECTS UPON DUPONT COMMON STOCK OF VARIOUS DISCOUNT VALUES AND DIVIDEND POLICIES*

MERGER AT SPECIFIED PERCENTAGE OF ADJUSTED NET ASSET VALUE (a)

	100%	97.5%	87.9% (h)	76.9% (i)
Earnings per share (b)	$7.31	$7.36	$7.56	$7.82
Percent change from 1971 (c)	−0.3%	+0.4%	+3.1%	+6.7%
Dividends per share, 68.6 percent payout (d,e)	$5.01	$5.05	$5.19	$5.36
Percent change from 1971 (c)	+0.2%	+1.0%	+3.8%	+7.2%
Dividends per share, 74 percent payout (d,e)	$5.41	$5.44	$5.59	$5.79
Percent change from 1971 (c)	+8.2%	+8.8%	+11.8%	+15.8%
Net number of DuPont common to be issued (retired)	110,696	(188,501)	(1,491,108)	(2,983,470)
Market value of net shares (j)				
April 28, 1972	$18,624,602	($31,715,293)	($250,878,920)	($501,968,820)
July 17, 1972	$18,209,492	($31,008,414)	($245,287,260)	($490,780,810)

* See assumptions on following pages, referenced by letters (a) through (j) on this table.

Assumptions

A. Adjusted net asset value as shown in DuPont Exhibit No. 5, pp. 6 and 7. Christiana's holding of DuPont common stock is valued at \$163.875, the average of the closing prices on the New York Stock Exchange, July 10 through 14, 1972. This value is also used to compute the number of DuPont shares to be issued to preferred and common stockholders of Christiana.

B. Earnings per share are based on net income of DuPont after the merger, calculated at \$347.6 million:

Actual 1971 net income earned on common stock Earnings of 4.46 percent on Christiana assets to be redeployed by DuPont:		\$346,500,000
Wilmington Trust Co. share	\$ 2,699,424	
News-Journal Co. share	24,260,000	
Cash, less current liabilities	5,981,367	
Claim for tax refund	11,723,013	
	44,663,804	
Less adjustment for handling tax refund claim	12,723,013	
Less expenses and taxes on sale of assets	7,619,606	
Less merger expenses	1,500,000	
	\$22,821,185	1,017,825

Preferred dividends saved by retiring Christiana's holding of 16,256 DuPont preferred shares, 16,256 x $4.50	73,152
	$347,590,977

Values of Christiana assets are from DuPont Exhibit No. 5, pp 4 and 6. The full amount of merger expenses is shown because these reduce the total extra assets available to DuPont. (4.46 percent is shown in Division's Exhibit 12, Exhibit 4—Kidder, Peabody).

C. Percentage changes in earnings and dividends per share are based on Christiana's 1971 earnings per share of $5.28 and dividend per share of $5.25, and DuPont's earnings per share of $7.33 and dividend of $5.00.

D. Payout ratios for DuPont of 68.6 percent and 74 percent are based on data for the previous five years. 68.6 percent is the average of the three lowest ratios; 74 percent approximates the highest ratio.

	1967	1968	1969	1970	1971
Payout ratio (%)	74.3	68.8	68.9	72.9	68.2

These data are computed from DuPont Exhibit No. 5, pp. C-3.

E. In these tables, dividends are maintained at specified proportions of earnings. These dividends change as earnings vary with differing discounts.

F. The computation of the premium, or increase in market value of Christiana shares, is based on the closing market price for DuPont and the closing bid price for Christiana on April 28, 1972, the day that

merger discussions were announced, and July 17, 1972, the day the proposed merger terms were announced.

G. Shown to three decimal places; calculations done with six or more decimal places. Formula for computation:

$$XR = \frac{\dfrac{(ANAV(1\text{-}d)) - 120CP}{DCSP}}{CCS},$$

where ANAV = adjusted net asset value ($2,223,-425,827)

CCS = number of shares outstanding of Christiana common stock (11,710,-103)

CP = number of shares outstanding of Christiana preferred stock (106,-500)

d = discount from adjusted net asset value (stated as a decimal)

DCSP = price of DuPont common stock ($163.875)

XR = exchange ratio (number of DuPont common for one Christiana).

H. 87.9 percent is shown because this is the percentage at which the dividend to Christiana common stock is the same before and after the merger.

I. 76.9 percent is shown because it portrays the effect of a 23.1 percent discount. This was the discount on April 28, 1972, based on mean market price and net asset value of Christiana (see Applicants' Joint Exhibit 1B, Exhibit 9—Morgan Stanley).

J. The market value of the net shares of DuPont to be issued or retired is computed using the closing market value for DuPont on April 28, 1972 and July 17, 1972.

APPENDIX D

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

No. 75-1100 RICHARD J. COLLINS, JR., PETITIONER, vs. SECURITIES AND EXCHANGE COMMISSION, RESPONDENT. No. 75-1262 LEWIS C. MURTAUGH, TRUSTEE FOR EMANUEL AND HELEN STEIB UNDER DECLARATION OF TRUST DATED 8-30-56, PETITIONER, vs. SECURITIES AND EXCHANGE COMMISSION, RESPONDENT. E. I. DU PONT DE NEMOURS AND COMPANY, INTERVENOR, CHRISTIANA SECURITIES COMPANY, INTERVENOR.	September Term, 1975 Petitions for Review of Orders of the Securities and Exchange Commission.

No. 75-1263 LEWIS C. MURTAUGH, TRUSTEE FOR EMANUEL AND HELEN STEIB UNDER DECLARATION OF TRUST DATED 8-30-56, PETITIONER, vs. SECURITIES AND EXCHANGE COMMISSION, RESPONDENT.	September Term, 1975 Petitions for Review of Orders of the Securities and Exchange Commission.

These causes came on to be heard on petitions for review of orders of the Securities and Exchange Commission, appendix and briefs of the respective parties and were argued by counsel.

On Consideration Whereof, it is now here ordered by this Court that the order of the said Commission granting the application to merge is accordingly set aside in accordance with the majority opinion of this Court.

And it is further ordered by this Court that costs will be taxed equally to Du Pont and Christiana in accordance with the majority opinion of this Court.

January 23, 1976

A true copy.

Attest:

/s/ Robert C. Tucker
Clerk, U. S. Court of Appeals, 8th Circuit.

March 8, 1976

APPENDIX E

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

75-1100

RICHARD J. COLLINS, JR.,
PETITIONER,

vs.

SECURITIES AND EXCHANGE COMMISSION,
RESPONDENT.

75-1262

LEWIS C. MURTAUGH, ETC.,
PETITIONER,

vs.

SECURITIES AND EXCHANGE COMMISSION,
RESPONDENT.

E. I. DU PONT DE NEMOURS AND COMPANY,
INTERVENOR,

CHRISTIANA SECURITIES COMPANY,
INTERVENOR.

75-1263

LEWIS C. MURTAUGH, ETC.,
PETITIONER,

vs.

SECURITIES AND EXCHANGE COMMISSION,
RESPONDENT.

September Term, 1975

Petitions for Review of an Order of the Securities and Exchange Commission

Respondent's and Intervenors' petitions for rehearing with suggestions for rehearing en banc have been considered by the Court and it is now here ordered that the petitions be, and they are hereby, denied by an equally divided Court.

February 26, 1976

APPENDIX F

The Investment Company Act of 1940, 54 Stat. 789, as amended, 15 U.S.C. 80a-1 *et seq.,* provides in pertinent part:

§ 80a-2. Definitions.

(a) When used in this subchapter, unless the context otherwise requires—

*** * * * ***

(2) "Affiliated company" means a company which is an affiliated person.

(3) "Affiliated person" of another person means (A) any person directly or indirectly owning, controlling, or holding with power to vote, 5 per centum or more of the outstanding voting securities of such other person; (B) any person 5 per centum or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote, by such other person; (C) any person directly or indirectly controlling, controlled by, or under common control with, such other person; (D) any officer, director, partner, copartner, or employee of such other person; (E) if such other person is an investment company, any investment adviser thereof or any member of an advisory board thereof; and (F) if such other person is an unincorporated investment company not having a board of directors, the depositor thereof.

*** * * * ***

§ 80a-17. Transactions of certain affiliated persons and underwriters.

(a) It shall be unlawful for any affiliated person or promoter of or principal underwriter for a

registered investment company (other than a company of the character described in section 80a-12 (d) (3) (A) and (B) of this title), or any affiliated person of such a person, promoter, or principal underwriter, acting as principal—

(1) knowingly to sell any security or other property to such registered company or to any company controlled by such registered company, unless such sale involves solely (A) securities of which the buyer is the issuer, (B) securities of which the seller is the issuer and which are part of a general offering to the holders of a class of its securities, or (C) securities deposited with the trustee of a unit investment trust or periodic payment plan by the depositor thereof;

(2) knowingly to purchase from such registered company, or from any company controlled by such registered company, any security or other property (except securities of which the seller is the issuer); or

(3) to borrow money or other property from such registered company or from any company controlled by such registered company (unless the borrower is controlled by the lender) except as permitted in section 80a-21 (b) of this title.

(b) Notwithstanding subsection (a) of this section, any person may file with the Commission an application for an order exempting a proposed transaction of the applicant from one or more provisions of said subsection. The Commission shall grant such application and issue such order of exemption if evidence establishes that—

(1) the terms of the proposed transaction, in-

cluding the consideration to be paid or received, are reasonable and fair and do not involve overreaching on the part of any person concerned;

(2) the proposed transaction is consistent with the policy of each registered investment company concerned, as recited in its registration statement and reports filed under this subchapter; and

(3) the proposed transaction is consistent with the general purposes of this subchapter.

§ 80a-42. Court review of orders.

(a) Any person or party aggrieved by an order issued by the Commission under this subchapter may obtain a review of such order in the United States court of appeals within any circuit wherein such person resides or has his principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the entry of such order, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall be forthwith transmitted by the clerk of the court to any member of the Commission or any officer thereof designated by the Commission for that purpose, and thereupon the Commission shall file in the court the record upon which the order complained of was entered, as provided in section 2112 of Title 28. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record shall be exclusive, to affirm, modify, or set

aside such order, in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission or unless there were reasonable grounds for failure so to do. The findings of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If application is made to the court for leave to adduce additional evidence, and it is shown to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceeding before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which, if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court affirming, modifying, or setting aside, in whole or in part, any such order of the Commission shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in section 1254 of Title 28.

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